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MILITARY RETIREMENT REFORM

HEARING

BEFORE THE

SUBCOMMITTEE ON MILITARY PERSONNEL

OF THE

COMMITTEE ON ARMED SERVICES
HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

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MILITARY RETIREMENT REFORM

HOUSE OF REPRESENTATIVES,
COMMITTEE ON ARMED SERVICES,
SUBCOMMITTEE ON MILITARY PERSONNEL,
Washington, DC, Tuesday, October 25, 2011.

The subcommittee met, pursuant to call, at 1:08 p.m. in room 2212, Rayburn House Office Building, Hon. Joe Wilson (chairman of the subcommittee) presiding.

OPENING STATEMENT OF HON. JOE WILSON, A REPRESENTATIVE FROM SOUTH CAROLINA, CHAIRMAN, SUBCOMMITTEE ON MILITARY PERSONNEL

Mr. WILSON. Good afternoon, and ladies and gentlemen, welcome.

Today the Military Personnel Subcommittee will address the subject of military retirement, an issue of immense importance to service members, and in turn to combat readiness.

I want to thank Congressman Dr. Joe Heck for recommending that this subcommittee conduct this hearing. Dr. Heck very astutely recognized that military retirement would be a pivotal issue in the coming months and that it was essential that this subcommittee address this issue expeditiously.

Thank you, Dr. Heck, for your insight and call to action.

The Defense Business Board, one element of the Department of Defense, was quick to present a major retirement reform proposal that set the tone of the retirement reform debate. The board's proposal would move the retirement system aggressively toward a private sector defined contribution system based on the personal investments of service members. The proposal received immediate criticism from service members and military associations.

The proposal is certainly a radical solution that would result in a significant reduction of retired benefits for all service members. As could be anticipated, the unveiling of the Defense Business Board proposal injected considerable uncertainty into the force, to include troops fighting in the wars in Iraq and Afghanistan. The proposal created an immediate morale firestorm as service members feared that senior members within the Department of Defense and the military departments were seriously considering its implementation.

We invited the Defense Business Board to testify today to face the arguments of their critics and explain the merits of their proposal, but they declined the invitation. I am concerned that the Defense Business Board knowingly elected to pursue a very controversial proposal with immediate negative consequences for morale and

combat readiness, and yet they were unwilling to come before this subcommittee and defend their actions.

In my view, their failure to appear speaks volumes about their own lack of conviction that their proposal is deserving of serious consideration.

Secretary of Defense Leon Panetta has been clear that retirement reform must be on the table for consideration as the Department of Defense contemplates the wide array of programs that will be considered for cuts to meet the budget reduction goals. I am pleased that the Secretary understood the morale problem that had been created by the Defense Business Board and announced his clear support for grandfathering the benefits to be provided to currently serving service members who have borne the burden of war over the last 10 years.

We simply cannot betray the trust of the service members who have performed with such courage and expertise in Afghanistan and Iraq.

I was disappointed that Secretary Panetta did not disavow the Defense Business Board proposal. That statement would have removed a major irritant to the force. I was, however, very pleased at General Dempsey's statement before the House Armed Services Committee that recognized the unique requirements of military service and that strongly asserted that the military requires a retirement system totally different from any civilian retirement program.

Today, we hope to learn more about the current positions of the Department of Defense and the military advocacy groups concerning the need to reform military retirement. I would like to welcome our witnesses, Dr. Jo Ann Rooney, the principal Deputy Under Secretary of Defense for Personnel and Readiness.

Dr. Rooney, this is your first opportunity to appear before the subcommittee. Welcome. I am certain we will be seeing more of you in the future.

Next, we have two highly respected professionals that are longstanding friends of the subcommittee: Ms. Virginia S. Penrod, the Deputy Assistant Secretary of Defense for Military Personnel Policy; and Colonel Steven P. Strobridge, USAF, retired, the Director of Government Relations of the Military Officers Association of America, MOAA.

Finally, let me introduce Mr. John Davis. He is a Marine, not a Marine veteran or a former Marine, a Marine. And so, we appreciate so much you being here today; the Director of Legislative Programs, Fleet Reserve Association.

Mr. Davis, this is also your first time as a witness before the subcommittee. Welcome.

Congresswoman Davis, you are recognized for your opening remarks.

[The prepared statement of Mr. Wilson can be found in the Appendix on page 29.]

**STATEMENT OF HON. SUSAN A. DAVIS, A REPRESENTATIVE
FROM CALIFORNIA, RANKING MEMBER, SUBCOMMITTEE ON
MILITARY PERSONNEL**

Mrs. DAVIS OF CALIFORNIA. Thank you. Thank you, Mr. Chairman.

And Dr. Rooney, welcome. I know that this is your first time testifying before the subcommittee and so we are glad to have you.

I also wanted to welcome Ms. Penrod, of course, and Colonel Strobbridge and Mr. Davis. Thank you all.

I look forward certainly to hearing your comments on potential reform to the military retirement system.

While we all know the concerns about the current state of our Nation's economy, the discussions on the condition and the future of military retirement are, once again, being raised. No surprise, I would suggest. Such discussions are not new. During previous economic downturns, focus has turned to the sustainability and the affordability of our military retirement programs.

However, for the most part, the current military retirement program was established over 60 years ago. So it is valid, I think, no matter how difficult, certainly difficult knowing the nature of the service and the sacrifice of the men and women who serve, it is still appropriate, I think, for us to ask ourselves whether the current program still meets the requirements it was set up to achieve, which, of course, we know is the focus of today's hearing.

Only 17 percent of the force actually completes a full 20 years of service in order to qualify for a non-disability retirement. And many have expressed concerns that the current program does not recognize the sacrifices of those who served during 10 years of conflict and may not stay the full 20 years to earn a retirement. Is it fair that that person, who may have been deployed once and stays to retirement is eligible for a lifetime benefit, while an individual who may have multiple deployments in a combat theater does not stay 20 years, that person walks away with nothing more than the admiration of a grateful nation.

When the 20-year retirement program was established, the life expectancy in 1949 for a white male was 66.2 years. For a black male, it was 58.9 years. Compared to the latest data available, the life expectancy in 2009 for a white male is 76.2 years and for a black male, 70.9 years.

So there is no doubt that Americans are living longer and more fuller lives, which means that an average individual who receives military retirement for 20 years of service will receive retirement for nearly twice as long in his adult life—his or her adult life.

In addition, many of those who retire at 20 years of service have gone on with an ability to seek another full career in a different field.

Changes to the personnel compensation programs, including the retirement system, often strikes fear in the force. So it is important, critically important, that we do not necessarily undermine the faith of those who are currently serving.

But we do have a responsibility to ensure that the compensation package that is provided to service members are meeting the needs of our Nation's national security, and that, of course, includes looking at the military retirement package.

Thank you, Mr. Chairman. This is an important hearing, and I look forward to our witnesses testifying today.

Thank you.

[The prepared statement of Mrs. Davis can be found in the Appendix on page 31.]

Mr. WILSON. Thank you, Ranking Member Davis.

I ask unanimous consent that the Defense Business Board report on their proposal to reform military retirement and a statement from the Reserve Officers Association be entered into the hearing record.

Hearing no objection, so ordered.

[The information referred to can be found in the Appendix on pages 61 and 96.]

Mr. WILSON. And at this time, we will proceed in order with our witnesses, beginning with Dr. Rooney.

**STATEMENT OF DR. JO ANN ROONEY, PRINCIPAL DEPUTY
UNDER SECRETARY OF DEFENSE FOR PERSONNEL AND
READINESS**

Dr. ROONEY. Good afternoon, Chairman Wilson, Ranking Member Davis and distinguished members of the subcommittee. Thank you for the opportunity to come before you on behalf of the women and men who so ably serve in our Nation's Armed Forces.

I am here today to speak to you about the military retirement system of our uniformed services. Since the military transitioned to an All-Volunteer Force, military compensation has been under continuous scrutiny. The primary goals of the military compensation system are to attract, retain, and eventually separate members so the United States forces can support the numerous missions both here and abroad and when called upon, succeed on the battlefield.

Even though some consider military benefits far-reaching, we must remain cognizant that they support the brave men and women who volunteer to defend this great Nation. Over time, while the military retirement system has remained relatively constant, pensions in the private sector have changed and more closely ally to support the more mobile workforce in that sector.

Unlike the private sector, the military services must grow most of their military workforce internally. It generally takes 15 to 20 years to develop the next generation of infantry battalion commanders and submarine captains. As a result, the Department must ensure military compensation, promotions and personnel policies all foster greater retention and longer careers necessary to create these experienced leaders.

This need for greater longevity and continuity suggests there are valid reasons why mirroring a private sector compensation package may not necessarily be the proper approach for the military.

However, the Department does believe that reviewing the retirement system is both a fair and reasonable endeavor, and over the past year has begun reviewing such retirement in the context of a total military compensation system.

The officer, enlisted, and civilian leadership of all Services, from the Active Duty, Reserve, and National Guard Components, as well as the U.S. Coast Guard, are participating in this review. The review is designed to be deliberate, careful, and pragmatic.

The Defense Business Board proposal is just one of several concepts that are being reviewed and modeled to determine the impact on recruitment and retention. The Department is working to strike the correct balance. This includes weighing the impact of a new system on recruiting and retention, considering the welfare of the individual service members and families, which includes grandfathering our existing force who took their oath under the current system, and acknowledging our responsibilities to the American taxpayer.

The Department needs to ensure any proposed changes do not break faith with the current members, or negatively impact the current force. Before proposing changes to the military retirement system or any part of the military pay and benefit structure, however, the Department is committed to conducting significant evaluation and in-depth analysis of any proposal.

The Department must ensure its ability to continue recruiting and retaining the highest quality members, and must understand to the fullest extent possible the impact of any changes on the future of the All-Volunteer Force.

Finally, while the Department acknowledges the military retirement system appears expensive, it is neither unaffordable nor spiraling out of control, as some would contend. The Department annually contributes amounts to the military retirement funds in accordance with the requirements set forth by the DOD [Department of Defense] Office of the Actuary. The contributions as a percentage of military basic pay are projected to remain relatively constant over time.

At this time, the Department does not have any specific proposals or recommendations ready to offer. Within the last month the President recommended forming a commission to review the military retirement system. If this commission is formed, the Department expects to provide significant input to the commission. The Department also expects that any proposals offered will be similarly presented to the Congress and to this committee for assessment and discussion.

I look forward to continuing to work with each of you as the Department moves ahead on this issue, and thank you again for the opportunity to testify, and for your continued support of our military members and their families.

I look forward to your questions.

[The prepared statement of Ms. Rooney can be found in the Appendix on page 32.]

Mr. WILSON. Thank you, Dr. Rooney.

We now proceed to Ms. Penrod.

**STATEMENT OF VEE PENROD, DEPUTY ASSISTANT
SECRETARY OF DEFENSE FOR MILITARY PERSONNEL POLICY**

Ms. PENROD. Good afternoon. Chairman Wilson, Ranking Member Davis, and distinguished members of the subcommittee, thank you for the opportunity to come before you to discuss the military retirement system for our uniformed services.

Dr. Rooney told you that the Department has begun a review of military retirement, and it is my office that has been tasked with this tremendously important undertaking. The purpose is to deter-

mine the impact and feasibility of restructuring the statutory and policy framework for military retirement.

We are aware that numerous commissions and studies have criticized the retirement system. However, I would like to point out that the current system has supported the most successful All-Volunteer Force in the world. The question now is whether the current system is still relevant in today's environment. If not, should it be modified to meet future requirements, and in a manner more in line with the private sector?

To ensure that in doing our review we get it right, we are considering the major aspects of military pay and benefits, along with the associated personnel and force management policies that have an impact on recruiting and maintaining the All-Volunteer Force. We are not looking at retirement in isolation.

Our work is not yet complete, so I am unable to report to you on the results of the review. However, I can assure you that sustaining the All-Volunteer Force and the men and women that so ably serve our Nation will be at the heart of whatever we do.

I look forward to your questions.

Thank you.

Mr. WILSON. Thank you, Ms. Penrod.

And Colonel Strobridge.

STATEMENT OF STEVE STROBRIDGE, DIRECTOR, GOVERNMENT RELATIONS, MILITARY OFFICERS ASSOCIATION OF AMERICA

Mr. STROBRIDGE. Thank you for this opportunity to present our views on military retirement concerns. We are grateful to the committee for standing up as champions, both now and in the past, to ensure military retirement incentives remain commensurate with the extraordinary demands of career service.

The primary purpose of the military retirement package is to induce top quality people to serve multiple decades under conditions few Americans are willing to endure for even one term. After a decade of war in which career service members deployed time after time after time with ever-increasing odds of coming home a changed person, we found it shockingly insensitive that some now seek to curtail their retirement package to, "make it more like civilian workers."

These are the primary incentives that have sustained the career force in peace and war. We are very concerned the recent proposals are aimed mainly at achieving budget savings, with scant regard to longer term damage to retention and readiness. The fact is we already have considerable history with military retirement cut-backs. Enactment of the high 3 year average basic pay system in 1980 cut retired pay by about 8 percent for subsequent entrants. Through the 1980s and 1990s, military pay raises were capped below private sector pay growth nearly every year, dramatically reducing lifetime retired pay for all the thousands of people who retired under those depressed pay tables.

And in 1986, Congress passed the so-called REDUX Retirement System that cut lifetime retired pay value by more than 25 percent for a 20-year military retiree. At that time, Secretary Weinberger, Secretary of Defense at the time, warned Congress that REDUX

would inevitably undermine retention and readiness, which proved true a decade later and Congress repealed it in 1999.

Recent proposals by the Defense Business Board and the 10th Quadrennial Review of Military Compensation envisioned far more dramatic cutbacks than REDUX did, delaying most retirement compensation until age 57 or 60, even though the Services don't want to keep most people anywhere near that long.

Both also proposed a vesting option for people who choose to leave early. We believe this is a formula for retention and readiness disaster. It would have destroyed the career force had it been in effect over the past 10 years. Some support vesting on a principle of fairness with private sector workers, but it is an odd concept in fairness indeed that would dramatically cut compensation for those who serve and sacrifice the longest to pay more for those who leave early.

Defense leaders have sought to quell concern in the field by saying they plan to grandfather the current force. But the REDUX experience proved that grandfathering doesn't avoid adverse retention effects, it only shifts them to the laps of future leaders. And in contrast to Secretary Weinberger's dire warnings about REDUX' threat to future readiness, current defense leaders have repeatedly expressed support for significant retirement cutbacks for future entrants, without a word about long-term retention risks.

In our view that is an abdication of their responsibility to protect future as well as current readiness. We are extremely grateful that this subcommittee and the full subcommittee have stood up to highlight those retention and readiness concerns to the "super committee" [Joint Select Committee on Deficit Reduction] when few others seemed so inclined.

That concludes my portion of the coalition statement, sir.

[The joint prepared statement of Mr. Strobridge and Mr. Davis can be found in the Appendix on page 38.]

Mr. WILSON. Thank you very much, Colonel.

And now we proceed to Lieutenant Davis.

STATEMENT OF JOHN DAVIS, DIRECTOR, LEGISLATIVE PROGRAMS, FLEET RESERVE ASSOCIATION

Mr. DAVIS. Thank you for the opportunity to testify on this important issue.

The All-Volunteer Force has successfully fought a protracted war due primarily to the dedication and patriotism of our men and women in uniform, but we should not underestimate the pay and benefits keeping the force sustained during this time of challenge.

Many wrongly believe that the uniformed services receive 50 percent of pay for 20 years of service, but that is not the reality. The retired pay calculation is based solely on the basic pay, excluding housing and subsistence allowances. Personnel with 20 years of service earn retired pay that replaces 34 to 37 percent of their gross cash pay and allowances. Any fair share accounting should acknowledge retirees that have already given under the past budget cuts.

Hundreds of thousands retired under depressed pay tables between the mid-1980s and the mid-2000s. They have already forfeited \$3,000 to \$5,000 a year for the rest of their lives. Regarding

the chained CPI [Consumer Price Index], some economists believe that the Consumer Price Index overstates inflation by failing to recognize that consumers change their behavior when prices rise sharply. When that happens, they say, people simply buy cheaper substitute products, such as chicken instead of beef, when the price rises.

It is more complicated with other substitutes. Is a compact car a substitute for a full-size car? Over time, this leads to a major change in living patterns. The chained CPI would reduce lifetime retired pay for an E-7 with 20 years of service by \$100,000. The TMC [The Military Coalition] opposes any kind of COLA [cost of living adjustment] cuts, because that violates the very purpose of COLAs, to protect the erosion of benefits by inflation.

Another proposal is to use the high five in lieu of the current high three. This would cut retired pay by 6 percent over 4 years. We oppose this, because it is just another way to devalue military service. The 10th QRMC [Quadrennial Review of Military Compensation] report suggests a 401(k)-type retirement payment starting at age 57 to 60. This would reduce retiree pay for an E7 with 20 years of service from \$24,000 a year, already a modest amount, to a ridiculous \$3,600 a year. This dramatic change would do grave harm for retention and recruiting.

A recent FRA [Fleet Reserve Association] survey indicates that 90 percent of respondents believe that if benefits were delayed until age 60, fewer people would join and they would serve shorter periods of time. The survey also indicates that more than 80 percent would leave the military sooner if military retirement was switched to a 401(k) plan, and 84 percent believe fewer people would join.

Career senior NCOs [noncommissioned officers] are the backbone of our military, and their leadership and guidance are invaluable as a result of many years of experience. Civilianizing benefits likely result in many of them leaving the military early, and these positions are very difficult to replace.

But the bottom line is the current retirement system is that it has worked as intended, sustaining a quality career force through good and bad budget times, through war and peace. It only stopped working after Congress cut it back in 1986. And that is a lesson we shouldn't have to relearn.

Thank you.

[The joint prepared statement of Mr. Davis and Mr. Strobridge can be found in the Appendix on page 38.]

Mr. WILSON. Thank you very much.

We will proceed now, and each member will have a 5-minute period of asking questions. And again, we have a person above reproach, Mike Higgins, who is going to be our timekeeper. And so, you can almost look at his face and tell when the 5 minutes is up.

I would like to begin with Dr. Rooney and Ms. Penrod. It is been widely reported that with the Defense Business Board reform proposal last summer, that there was a great deal of distress among career service members. DOD's reluctance to disavow the proposal has given rise to concern that there is strong support at DOD for such reforms.

With this report, does DOD intend to support the Defense Business Board proposal? And then, it has already been identified by both of you that there are studies underway as to how this proposal will affect retention. When should we expect a report on the effect on retention?

Dr. ROONEY. Yes, sir. In regards to our posture on the Defense Business Board, you indicated that early on we did not come out adamantly against it. But I believe that recent statements by the Secretary, the Chairman, and even in our opening statements clearly indicated that we are seeing the Defense Business Board proposal as just one data point for consideration in review as we are looking at the overall retirement and compensation system.

Again, the key factor for us is that any change or any system, frankly, must ensure that we are able to recruit and retain the All-Volunteer Force and not at all damage the current faith that the troops have in us. So that report has some very strong limitations. It is a data point for us and we see it just as that, as a data point.

You also asked where are we in terms of a proposal coming forward. And as Ms. Penrod indicated, we have a group that is currently looking at a number of alternatives. And we are working closely with the RAND Corporation to also help us in the analysis of that, again with the idea that recruiting and retention are key factors to consider in any kind of proposal.

So at this point we don't have a specific date. However, with the President's proposed commission, if that would stand up in the springtime should that go forward, we would be prepared at that point in time to be very much informing the conversation with them.

Mr. WILSON. And Ms. Penrod.

Ms. PENROD. Yes. As Dr. Rooney stated, we are working with RAND to model any proposals or changes to the current retirement program. We preliminarily have the final report of the DBB [Defense Business Board], and it does have a negative impact on retention. That is what it is showing us at this time. We are not complete with that review, but again, as Dr. Rooney stated, it is a data point. And we will take that report and it will inform as our review goes along.

Mr. WILSON. I thank both of you. I was very impressed, Colonel and Mr. Davis, the facts that you pointed out. People should know how this affects individuals. And with that in mind, what is your reaction that the retirement reform is unavoidable because it is fiscally unsustainable? What would be your response, each of you?

Mr. STROBRIDGE. The testimony we have heard here today from the DOD witnesses kind of refutes that, where they said it is neither spiraling out of control, nor unsustainable. Their projection is that it is going to be about the same percentage of basic pay into the future. I think the committee has statistics that has shown that retirement costs as a percentage of the DOD budget have been relatively stable over time.

The first time I worked on military retirement was in 1977 and we showed projections at that time that critics were pointing out that it was going to be the system would go broke by the year 2000. Well, we are still here and we just fought a war since the year 2000, so I kind of pooh-pooh those kinds of ideas.

Mr. WILSON. Thank you.

Mr. Davis.

Mr. DAVIS. Well, I would certainly agree with everything Colonel Strobridge just said. And I would just add that, you know, the price of military retirement, the price of military benefits, is really part of the cost of fighting a war that we are currently involved with, and the price of defending our Nation, and should be put in that category as well.

Mr. WILSON. And I want to thank all of you as I conclude, because I can see your appreciation of the career NCOs, the junior officers. We can, "get new recruits," but the expertise must be maintained for the security of our country, of our NCOs and junior officers.

Proceed to Congresswoman Davis.

Mrs. DAVIS OF CALIFORNIA. Thank you, Mr. Chairman. And again, thank you all for being here.

I wonder if you could address the issue of fairness? As I mentioned in my opening statement, that we have certainly hundreds, thousands of our military personnel who serve out the 20 years, though they may only deploy once, if at all, in a conflict theater, versus those who deploy on many occasions. Certainly we know in the last 10 years that is quite common, and yet do not serve the full 20 years.

How do you think we should go about looking at that issue? And do you think it is one of fairness, or is it, you know, just the way it is?

Doctor, do you want to start, or that is fine.

For all of you.

Mr. STROBRIDGE. To me the key purpose on the retirement system is sustaining the career force. National defense comes first. I am all in favor of fairness. I have built my career on arguing issues of fairness. But you have to sustain the system through peace and war, through good budget times, through bad budget times.

And we all have seen periods in the past where we have pulled out all the stops to retain people, when we have had service conditions so terrible, or an economy that was so strong, that we had to raise retention bonuses, we had to pay, you know, extra things. Those are going to happen in the future as well.

And when we acknowledge that the military service conditions are unique and vastly different from civilian conditions, the fact that we can only get 17 percent of enlisted people to stay for the current system to me speaks for itself about the arduousness of the career and the few people who are willing to endure that for a long time.

To then turn around and say, "But we need to pay more to people who leave," to me, any time you have a vesting system it by definition detracts from a career incentive. It can't do anything else. And in bad budget times, it leaves the Government bidding against itself for their services, which only drives up costs.

So to me if you want to talk fairness, the first thing we have to do is be fair to the people who suffer and sacrifice the longest, and that is the career person. And the last thing we should be doing is cutting their package to fund a better package for people who leave.

Mrs. DAVIS OF CALIFORNIA. All right.

Dr. Rooney, did you want—

Dr. ROONEY. Certainly. When we are looking at fairness, and you brought up a good point, because you were even talking about the range of people and deployments and all. And that is why in my opening statement, and you have heard other comments from the Department of Defense, that we look at compensation as a total package of which retirement is only one segment of it.

So across that, whether it is basic pay, hazardous duty pay, imminent danger pay, all of the different aspects that go into compensation, that is how we get that balance of fairness.

The other thing in terms of the overall system for fairness is when people come into the military they understand this system. They come in knowing what the various pieces are, and as a result, they are feeling because we are viewing it from not only basic pay, but all the tenets of compensation up to retirement, that we do get a balance of fairness.

The point you did bring up though, in terms of should we be adding a component to retirement to compensate for those people less than 20 years, that is one of the reasons that we are saying it is very prudent to be looking at military retirement as part of the overall compensation to determine if in fact there is something in that aspect that we need to look at more closely.

Mrs. DAVIS OF CALIFORNIA. Thank you. And in the little time left, if Mr. Davis, did you want to comment?

Mr. DAVIS. Yes, I just want to point out that we did a survey and that was one of the questions that we asked 350 Active Duty personnel, do you think it is fair for people that, you know, to get a pension, you have to serve 20 years? And 81 percent of them thought it was fair.

So, you know, in the ranks of the military, apparently there is no feeling that, gee, you know, if I serve 10 years and get out, it is unfair because someone else serves 20 years and they get a pension and I get nothing.

And I also would like to just point out too, it is not under the jurisdiction of this subcommittee, but if someone serves 10 or 12 years, of course, they are not—they are then under the jurisdiction of the Veterans committee. And they do have benefits, of course, such as the G.I. Bill and a whole latitude of things that they can use basically to get benefits from their service.

Mrs. DAVIS OF CALIFORNIA. All right. Thank you.

Yes, Ms. Penrod, did you want to comment?

Ms. PENROD. I think I agree with you, Congresswoman Davis, that it is the 20-year retirement has sustained an All-Volunteer Force, but I believe we should look at it. We have a different cohort coming in every year. How do we know what the future will look like, what people are looking for in a retirement system?

It may make the military more enticing to come in if an individual thinks that they may have something they could take with them. Also, even though you have the G.I. bill, I think that is an outstanding benefit, you still have an individual that will be separated possibly during drawdown with 12 years of service. And so, I think we need to look at that, and that is what we are going to do, is look at the whole program.

Mrs. DAVIS OF CALIFORNIA. Thank you. Thank you very much.

Thank you, Mr. Chairman.

Mr. WILSON. Thank you.

And we proceed to Mr. Coffman of Colorado.

Mr. COFFMAN. Thank you, Mr. Chairman.

And I guess my first question is I think some of the testimony today had referenced that it is a relatively low percentage of payroll that supports the retirement system. But nobody has said what that is, and I am wondering if somebody could give me a percentage number?

Dr. ROONEY. At this point, we have some of the numbers. I would like to take that for the record, please, sir.

[The information referred to can be found in the Appendix on page 103.]

Mr. COFFMAN. Very well.

You know, I just think that there are—first of all, I agreed with the Secretary of Defense, when he testified before the House Armed Services Committee recently, and he said that whatever reforms we do, should not affect those who are currently on Active Duty and went in with the understanding that this is what the system is when they, in fact, enlisted or were commissioned in the Armed Forces of the United States.

However, with that said, and myself being a retiree from a kind of an Active Duty and Reserve combination, that I remember as I was approaching the 20th year mark—and when you are a Reservist and if you are injured, not when you are on Active Duty, it is not considered line of duty, “not misconduct” would be the category. And you don’t fall into that, you report back for duty.

I was in the Marine Corps Reserve in that weekend. And if you are determined that you can’t do what they ask you to do, because you have sustained an injury skiing, then you are automatically out. And there is nothing there for you. And I gave up skiing in Colorado as I got closer to that 20-year mark, just to make sure that nothing happened there, as I got close to that.

I just think that there—we need to take a look at that—not so much the Reservists, but I think the Active Duty Component. And I disagree with the notion that we ought to go in the direction of all defined contribution. I just think that we are asking our service members to give a lot. And I think that there needs to be a component of certainty in that.

So perhaps a more bifurcated approach that would be defined benefit with an element of defined contribution for those who would enter the Armed Forces after the effective date of the new system, when it was put in place. So I just think that this system needs to be reformed, it needs to be revised.

It is something my father was under this system as a retired Army master sergeant, was in World War II and Korean veteran, and I think that as Congresswoman Davis has said, things certainly have changed since then in terms of life expectancies and a number of other issues. So I just think that everything we ought to look at.

But I understand the Defense Advisory Board only looked at one issue, if I understand that, only came across with one suggestion,

and that was just completely defined contribution. Is that my understanding?

Dr. ROONEY. Yes, that is the only proposal we have seen, is one that is a defined contribution.

Mr. COFFMAN. Yes, and I am surprised by that and disappointed by that. I just think that, I mean, if you look at the system for Federal civil service, or for Members of Congress, I think for Members of Congress and their staffs, it is 1.7 percent a year for the first 20 years. It is 1 percent thereafter for the next 10 years.

And there is a Thrift Savings Plan, which is the defined contribution part, which is there for all Federal employees. And it is a lower, I think, factor. I can't remember what it is for Federal employees.

But the difference between Federal employees and the military or members of Congress, if you will—and I am not a fan of our retirement system. I think it ought to go. But for the military it is the fact that they don't have—and we don't really want them to have—the sort of career protections that Federal civil service has.

And so, when you compare the two retirement systems, I think you need to recognize that in the military system. And it has to complement the fact that they are all at-will employees when making determinations about retirement.

So I look forward to working with you, or all of you, in terms of coming up with a new system. I am certainly not going to say that the old system ought to be replicated going forward. I don't believe that. But coming up with a new system. And I do believe that we need to look at, in particular, those folks that serve less than 20 years, that I think that they ought to accrue something for that.

And I think there ought to, in the new system, again for those who are not members of the Armed Forces yet, I think we ought to look at the notion that should you begin drawing the defined benefit portion of your retirement, right at the end of the 20-year mark, or whatever the mark is. So I think that there are a number of issues that ought to be on the table.

With that, Mr. Chairman, I yield back.

Mr. WILSON. Thank you very much.

We now proceed to Congressman Dr. Joe Heck.

Dr. HECK. Thank you, Mr. Chairman. I especially want to thank you for pulling this hearing together so quickly after my request.

I want to thank all the panelists for being here today and providing your testimony.

You know, I agree that it is certainly reasonable to review the pay and benefits in the retirement system of our Armed Services, but where I disagree is when the Defense Business Board's proposal is released publicly without much information given to our men and women who are currently serving in harm's way.

And then I receive the e-mails and phone calls from folks wondering what is going on with their potential retirement and hearing first-hand what the impact was on morale in theater, not that they are not already worried enough about whether or not they are going to get their next paycheck back home, so their wife can make the mortgage. But now they are worried about what is going to happen when they hit their 20-year mark and what is going to go on with their potential retirement.

You know, the question of is the current benefits package or the current retirement relevant, I think, poses a concern in that how do you define relevance? You know? And I hope that that is not a euphemism for the costs associated with the retirement program, especially when only 17 percent of the folks who spend their lifetime in, you know, enter the service wind up qualifying for a full retirement.

I know it is hard enough under these fiscal times when we are trying to figure out how Department of Defense is going to meet the \$450 billion reductions over 10 years that this Administration has already called for.

But is this review of benefits and pay taking place in a vacuum? Or, is it being looked at in conjunction with the amounts that we spend on basing and facilities and the amount that we are spending on hardware and weapons systems? Or, is each one of these things being reviewed in a silo?

Because my concern is we can have the best piece of equipment, the best weapon system, but if we don't have the person to gain the site picture or pull the trigger, like the great pilots I have at Creech Air Force Base, manning the RPAs [remotely piloted aircraft] now in theater, that weapon system really doesn't do anything.

So is this being done in a vacuum, or is it being looked at across-the-board in the entire DOD budget?

Dr. ROONEY. Sir, I will be happy to comment on that.

No, it is not being looked at in a vacuum. We are looking at, as you said, the challenge that we have for budget cuts, but as not just across-the-board cuts or arbitrary cuts, but very strategically looking to what does our future force need to look like? And how then, once we determine that future force, how do we attract and retain the best people using compensation as the tool to be able to again support that All-Volunteer Force, keep our current troops, the faith of them, but also going forward to attract and retain.

So it is part of an overall strategic look at how we are going to face not only the budget challenges, but our challenges as a Department of Defense going forward.

Dr. HECK. Well, and I appreciate what Colonel Strobridge stated, having lived through the years of having to give recruitment bonuses or incentive bonuses, and then using stop-loss to keep people in. And now we are getting to the point where we are cutting the Active Duty force in both the Army and the Marine Corps.

So how does that play into this decision? I mean, we are already trying to downsize the force on purpose, and now we are talking about potentially changing the retirement program, which may cause an additional exodus?

Dr. ROONEY. Actually, sir, when I was indicating strategic, I do mean we are taking into consideration that we are doing a force drawdown. But we are also looking forward and acknowledging that in addition to keeping the faith with our current forces, we will be recruiting new forces going forward.

You mentioned some specific capabilities at Creech. So that is part of the area that we know our forces for the future will rely on new technologies, and we may have new requirements for recruiting those folks.

So as we are looking at what does this force look like, what are the attributes, we just want to make sure that our overall compensation package, of which the retirement is one, is the right combination of package.

And that is why we are saying that there is no decision that has been made on any component of that. But as the Secretary has said several times, we must put everything on the table because that is the prudent way to approach this challenge.

Dr. HECK. And in my limited time just a quick final question.

Has there been set a dollar figure that is supposed to be attained, either in retirement or overall in pay and benefits, in trying to help balance the DOD budget?

Dr. ROONEY. Not a specific one.

Dr. HECK. Thank you.

Thank you, Mr. Chair. Again, thank you for holding this hearing. And I yield back.

Mr. WILSON. Thank you, Doctor.

We proceed to Congressman Allen West of Florida.

Mr. WEST. Thank you, Mr. Chairman, and Madam Ranking Member, as well.

And thanks for the panel for being here.

And I guess I am one of those guys that the ranking member talked about that did do a career in the military and was young enough to continue on to have a, I guess, a second career. Which is kind of a laughable hypocrisy, in that 22 years in the United States military Active Duty I got a 55 percent retirement. And I believe in 5 years on this side I could get vested into an even greater retirement. So we can talk about that later.

But as I sit here today, I am very concerned, and it takes me back to the quote by George Washington, where George Washington talked about how future generations will regard their service to this Nation based upon how well we treat our veterans.

And I recall my father, who was a World War II veteran, sitting down and talking to me about how great it would be to serve a career in the military.

So when I look at a career in the military, when I look at people that are serving in our military, that is a defined contribution. And on the backside, I think that we should be giving them a defined benefit for that contribution because of what they do.

Now, my first question is, do we still have the Thrift Savings program, the Thrift Savings Plan, for those men and women out there who, you know, may just serve, you know, 5 years. And while they are in a combat theater they are allowed to go into that Thrift Savings Plan, so they can put—start putting away some money?

Ms. PENROD. Yes, Congressman West, we continue to have the Thrift Savings Plan.

Mr. WEST. Okay. Now, when we talk about comparing military service to the civilian sector, does the private sector, civilian sector have something that is equal to the Uniform Code of Military Justice?

Dr. ROONEY. No, sir, they do not.

Mr. WEST. Okay. In the private sector, other than being a professional athlete, does your position and your ability to progress through the ranks depend on your physical abilities? And do we

mandate that people have to get up at 6:00 in the morning regardless of the conditions thereof to participate in physical training and activity?

Ms. PENROD. Well, Congressman, I cannot comment on private sector employment. However, I can say that I think we all agree that the sacrifices are not the same for our military personnel as they are for our private sector civilians.

Mr. WEST. And I think that is my biggest concern, is that what we ask the men and women to do, ever since those men answered the call of arms at Lexington and Concord, is different from someone just going to a bank, or different from someone even coming here to work on Capitol Hill.

So it is a very dangerous road when we start to go down the comparative analysis of the private sector or business sector to the United States military. So I ask that we be very careful about that, because I think that we are already starting to make some decisions thereof.

How many people in the panel do you remember what happened after Desert Shield/Desert Storm when we all of a sudden offered people money to exit the United States military? I do. Have you all done any research as far as the degradation of leadership, which is something that General Martin Dempsey talked about when he came and testified before us up here a couple of weeks ago? Have we looked at that and what could happen as far as the progression of leadership?

Dr. ROONEY. Yes. I believe General Dempsey used the term "hollowing of the force," and the Secretary has also talked about that that is something we have learned many lessons from the past. And we will not do anything to our compensation system so that we end up with that hollowed force.

Mr. WEST. Okay. Any comments, Colonel?

Mr. DAVIS. I would just like to say I know what you are saying about that. And that, you know, from the enlisted side, you have, you know, senior enlisted people, a sergeant major, whatever—

Mr. WEST. You need first sergeants and sergeant majors.

Mr. DAVIS. You need first sergeants, to nothing else to they, those people, combined with the junior officers, have, you know, a hard-charging junior officer. But you also have a senior enlisted person who can, you know, have a wealth of experience with the military, 20 or 30 years, that they can, you know, explain things to the junior officer, can call on them for their experience. And that makes a very powerful combination.

Mr. WEST. And I will testify to that, as a young stupid second lieutenant when I first came in.

Colonel, you have anything you want to add?

Mr. STROBRIDGE. Yes, sir. I think so many of these things and these analyses treat people in the context of, "human resources," as if they were widgets in a box instead of thinking, planning human beings.

And when we model—I have got a lot of, you know, doing a lot of studies, working with RAND. I spent a lot of time working with RAND.

The problem with all these is the models don't include things you can't quantify, such as sacrifice, such as time away from home.

They include all the money people spend, you know, they can measure behavior. But they don't talk about—there is nothing in the model that accommodates the chance that we might go to war tomorrow, and you might be going to Iraq every other year for the next 10 years.

There is nothing in there that accommodates for the fact that we might do the opposite. We might stop a war or we might have a budget-driven drawdown and you have built your plans on staying for a career, and all of a sudden we are going to force you out.

And those are the kinds of things that, you know, service leaders are always seeking additional flexibility to be able to micromanage the force. And the only thing we know about those kinds of plans is whatever you plan for 5 or 10 years is going to be wrong, because the world is going to change your plan for you.

And to us, that is one thing, when you have a very powerful career incentive like the 20-year retirement plan, it is very resistant to day-to-day manipulation. And that is a good thing.

Mr. WEST. Thank you.

And I just hope that our fiscal irresponsibility on this side does not become borne on the backs of our men and women in uniform or their families.

And with that being said, I yield back, Mr. Chairman.

Mr. WILSON. Thank you very much.

And Congressman Scott of Georgia.

Mr. SCOTT. Thank you, Mr. Chairman.

And I am going to focus more on the gentlemen, ladies, with my questions, if I may.

And I would like to focus, if we could, on the 80 percent—83 percent that get nothing. And, Colonel, you were just talking about the potential of somebody to go overseas every other year for the next 10 years, five tours, and then you have a drawdown or a force reduction. And the bottom line is that person would not qualify even though they may have wanted to stay for 20 years, they would get nothing, is that correct?

Mr. STROBRIDGE. Well, no, I don't think that is correct. When we have these kinds of drawdowns, for example, Congressman West was talking about what happened in the 1990s. We had very special programs to provide additional incentives to try to entice people to separate voluntarily. For people with 15 to 19 years, Congress authorized an early retirement program.

As difficult as those things are, that was probably the best example of the kind of thing that can be done.

Now, the challenge is the drawdown that is coming up in this fiscal environment, I think it is going to be a lot tougher for Congress to authorize those kinds of programs. So we are going to be seeing less incentives. There will be some incentives, but probably less.

Mr. SCOTT. Of the 17 percent who receive the benefits from the 20 years, what percentage of them are enlisted?

Mr. STROBRIDGE. The—

Mr. SCOTT. Seventeen percent of the men and women qualify.

Mr. STROBRIDGE. Of the people who stay for a career?

Mr. SCOTT. Right.

Mr. STROBRIDGE. What percentage are enlisted? Probably about 70 percent, I would think.

Mr. SCOTT. Okay. So 70 percent are enlisted.

I guess my question is, you know, I hear your objection to having—you object to having any other plan, is that correct?

Mr. STROBRIDGE. No, I don't object to having any other plan. I object on the face of it to saying that because civilians do these things, that the military should, too.

The military is a very different system. It is built to serve a very different purpose. And so to me, it has to start with that uniqueness and not assume that what happens in the private sector is in any piece is a good thing. It needs to be evaluated on its own merits.

Mr. SCOTT. Well I certainly agree with you that they are different, but I do think that it is necessary for this committee and for us as a Congress to do something that helps that 83 percent who don't qualify under the 20 years. And you know, there are many of them that have served many tours overseas. And I understand that we have to have our experience in our officers and maintaining those things.

But I also I will tell you I do think that we need to remember those 83 percent of the people who have spent their time and their family's time and contributed a great deal to the freedoms that we enjoy in this country. And I see nothing wrong with them being free to choose a different retirement plan on their own will.

So we will work on that as time goes on.

I would ask, Mr. Davis, would you give me that math again that you used, where you said 3,000 was the last number, and maybe 24,000 was the first in your presentation.

Mr. DAVIS. That was the 24,600 for an E7 with 20 years as compared to taking the plan proposed by the 10th QRMC, which was to put them into a 401(k). But they wouldn't be able to get that until age 57 to 60. I believe it came out to \$3,600 a year, the 401(k) benefit.

Mr. SCOTT. How many years would they have contributed to that 401? Could you just share that math with the committee? I would like to—

Mr. STROBRIDGE. If I could clarify that calculation?

You are referring to a chart that we made. The \$3,600 would be the initial value of the defined benefit retired pay. In other words, the 24,000 would be reduced by 5 percent for each year the person left before age 57.

And assuming an enlisted person leaves at age 40, that means it would be reduced 85 percent. So the defined benefit contribution, or the defined benefit portion, would be \$3,600 a year. There would be some additional amount that person would receive from their Thrift Savings Plan that would be in the range of \$10 to \$13,000 that they could start drawing at age 60.

Mr. SCOTT. But that would be contingent upon how much money they put into the direct savings plan?

Mr. STROBRIDGE. Correct.

Mr. SCOTT. I would like, if I could see that math on that? I would just like to see the math on that.

Mr. STROBRIDGE. Yes, sir, we have a chart on that in our formal statement. I can get it to you.

Mr. SCOTT. Great, thank you.

Mr. WILSON. Thank you very much.

We now proceed to Congresswoman Hartzler of Missouri.

Mrs. HARTZLER. Thank you, Mr. Chairman, Ranking Member Davis. Appreciate all of you being here.

I wanted to start, if I could, with Colonel and ask you to expand a little bit more on your comment earlier that you don't think grandfathering in, if there was a new plan, you don't support, you know, having a new plan and just grandfathering in current members of the military. And could you expand on your concerns?

Mr. STROBRIDGE. Sure. I think my point was people look at grandfathering is a panacea that everything will be okay as long as we grandfather the current force.

I have a letter. The letter that I referred to that Casper Weinberger wrote back in 1985 that went to Tip O'Neill expressing concern about the REDUX plan Congress was about to enact. And he spoke, that letter spoke very eloquently on grandfathering. If you don't mind, I would like to read it for a moment.

It says, "While the changes we have been required to submit technically affect only future entrants, we expect an insidious and immediate effect of the morale of the current force. No matter how the reduction is packaged, it communicates the same message, that is, the perception that there is an erosion in support from the American people for the service men and women for whom we call upon to ensure our safety.

"It says in absolute terms that the unique and dangerous and vital sacrifices they routinely make are not worth the taxpayers' dollars they receive, which is not overly generous."

Now, the issue, there was a line in there where he said, basically, you have two categories of people serving side by side who each know that they have different benefits. And that was a very accurate predictor of what happened in the 1990s, where you had the people who were trying to reenlist people say either they mislead them and tell them what the benefit they have which, when the people find out that that wasn't true, they get particularly upset. Or, you have these people saying, I am sorry, but the benefit you have is not what your predecessors have.

There is just no way, as those people go through 20 years serving together, that that doesn't become a burr under their saddle.

Mrs. HARTZLER. Okay. So you are not for any changes at all? You want to keep the system the way it is now forever?

Mr. STROBRIDGE. It is probably not realistic to say there will never be any changes at all. The thing that I think we would have to—and very frankly, there would probably end up being budget-driven changes of some type. I think we have to start from the standpoint that we have tried some of these things before. The one that we know was a tragic failure was the REDUX system, which compared to the things that are on the table today was pretty modest.

Mrs. HARTZLER. All right. Could I hear from the Department of Defense representatives on why you initiated this whole process? What is—why do you think there needs to be some changes? What is the rationale?

Dr. ROONEY. It is actually multiple purpose. One is that we are looking to our future force. And again, we talked about such con-

cepts as we don't want to hollow out the force as we are changing. We know we are facing drawdowns. We also know that our future force very much can look different in terms of the type of force we must recruit, the qualifications, the technical aspects. So right there is we are doing that review that prompted us to say are we sure we have the correct pay/benefits/compensation package going forward?

The timing of that review, and not only the speed, but the deliberateness of it clearly ties in to our budget concerns going forward. And the budget we must meet and the reductions we must meet. So all of that is coming together at the same time. And again, because we are trying to view all of the budget reductions strategically, and as though they are interconnected, this does become part of that discussion, but is not solely driven because it is a budget exercise.

Mrs. HARTZLER. Okay. I wanted to jump to a concern that I have heard at home and see if any discussion is taking place with this. There are about 30 seconds left.

But is there any incentive currently in the system, which I don't believe there is, to encourage people to stay 30 years?

Some of the concerns I have heard from some of my retired military at home was that right now, we have many people retiring at 20 years and we are losing that knowledge and all that experience.

So, is there anything being looked at to encourage people to stay longer?

Ms. PENROD. Actually, as we look at our review, we look at the whole force profile, and agree the 20-year retirement pulls people with 20 and it is cliff-vested. And the force today of the Services, they have built their force profile around that behavior.

You continue to earn 2.5 percentage points for every year you stay in the military up to 100 percent, or over 100 percent. So we do have changes that happened several years ago as far as retirement. But that will be part of your review. We have a model, as Steve said, RAND has a very strong model to look at the impacts on retention, but that just informs the process.

We also have our senior enlisted advisers are part of the working group. All Services are represented. Coast Guard is represented. Guard and Reserve are represented. So that is where you have that human piece of this review and the experience.

Mrs. HARTZLER. Thank you. And I just encourage all of you as you go through this process to continue to get input from as many people as possible affected by this, as well as Members of Congress. This is a very, very important topic to certainly people in my district, but to our national security. And so, no change should be made lightly, obviously.

So thank you for what you are doing. Thank you for the input, and thank you for your service.

Thank you, Mr. Chairman.

Mr. WILSON. Thank you, Ms. Hartzler.

Mrs. Davis, do you have another question?

Mrs. DAVIS OF CALIFORNIA. Thank you, Mr. Chairman. I wasn't sure if we were going to have another round, but there are a few questions.

And one is really to Mr. Strobridge and Mr. Davis. I know how difficult this is in getting input from all the people who you speak to. But I am wondering within this discussion whether there are really some priorities, perhaps, that had been identified? Whether there were some areas in which you feel that you could find savings? Can you prioritize any of the benefits for us? What should be protected? What could be modified, reduced or eliminated?

Acknowledging, of course, that you would rather not see any reductions at all, and that even the targeting here is problematic. But are there some areas in which you could define for the committee that might be helpful?

Mr. STROBRIDGE. Well, I think one thing you have to recognize is we are here representing 34 organizations, and that does require a wide diversity. We did have some difference of opinions on healthcare, on the TRICARE fees. In the end, you know, the kinds of differences we were talking about were \$5 a month, you know, and those were very significant within the coalition.

We had a lot of debates over those, you know, whether we should just say no changes.

I think there are a reasonable number of groups that would say no changes, the system works. You know, this is what people were promised, we ought to stick with it. I think there are people who would be willing to discuss those things, but I think that it is much tougher on retirement, very frankly, than healthcare. And even healthcare, when we were talking about that, we were talking about relatively small differentials.

The kinds of things in healthcare that are on the table now, which were very disappointing to us who did buy into a \$2 increase on pharmacy fees, to then have the Administration turn around before that even gets enacted and say, you know what, no. We are going to raise that to \$40. That is a big problem.

And that raises some serious credibility issues that, you know, give, you know, support to the idea that give an inch, you take a mile. So that is a very significant concern.

Retirement, every retirement plan that has been put forth for the past 4 or 5 years, when you go back to look at the Defense Advisory Committee for Military Compensation proposal, the QRMC proposal, the Defense Business Board proposal, all of those entailed radical changes, way worse than the REDUX that failed.

And so, when you see that, I think we all get our arms—our, you know, hair on fire and say, “I am sorry, you are just starting from the wrong place.” We are starting from how much money can we take out of it, when what we should be starting for is what should people earn for a career of service and sacrifice under conditions that can range anywhere up to and including deploying every other year for 10 years, or giving up your life, or coming back with PTSD [post-traumatic stress disorder] and TBI [traumatic brain injury] and not only your life, but your family’s life is going to be changed forever?

Those are the kinds of things, as Congressman West said, that we believe have to be counted as the contribution. That is what people really pay in a career of service and sacrifice.

Mrs. DAVIS OF CALIFORNIA. Thank you. I certainly appreciate what you are saying. I think we all do. I appreciate that. If there are things that you can offer to us, that is always helpful.

Mr. Davis, I don't know if you wanted to comment further. And I had one other question.

Mr. DAVIS. I just wanted to, you know, second his information. But also, just to remember when looking at the retirement system, I think it is important to remember that, you know, our Armed Services are there to fight wars, and war is a young man's or woman's profession. And I look back at some of the stuff I did when I was in the Marines, carrying artillery shells and all that kind of activity that you do. I probably couldn't be able to do it today.

So, you know, when you think about it, you know, it is a young man's or woman's profession and the retirement system should reflect that.

Mrs. DAVIS OF CALIFORNIA. Yes, thank you. If I may just for our Department of Defense witnesses, and you can do this certainly for the record, because my time is almost up. Could you also help us understand where you are looking to address other increased costs and expenditures that we have in our contracted services?

I would like to know what we are doing about that, because the concern, of course, is that we are looking here at retirement benefits and other benefits to the military, and yet we see that despite the fact that perhaps you are trying to look at some of those costs, at the same time we are maybe doing away with some services from our civilian personnel that we would have to go back and then contract with the outside.

And I would like to know what else you are doing? How are you going about addressing those issues so we are talking about costs across the board? And I know in response to one of the other questions, you did say this is not the only thing we are looking at, of course. But I would like to know how you are going about that and how far along we are in looking at a lot of the contracted services that also cost us a great deal of money?

Thank you very much.

Dr. ROONEY. Certainly, we will take that for the record, given our time.

Thank you, Congresswoman.

[The information referred to can be found in the Appendix on page 103.]

Mr. WILSON. Thank you very much.

During our whole debate, I was impressed several times, it was referenced about military families. And as we are looking into the issues of retirement, the military families truly are of service and sacrifice.

And I just hope that every effort is made to work with military families and get their input, because they really truly sacrifice so much, but they are counting on a very positive career, a very fulfilling career for their spouses and for themselves.

A question that I would have is for Colonel Strobridge and Mr. Davis. Has the Department of Defense consulted with your organizations, Fleet Reserve, MOAA? Or, have they consulted with other military organizations and associations for their input on this issue of retirement reform?

Mr. STROBRIDGE. Not to date, no sir. I think there are probably people who would prefer that they didn't.

Mr. WILSON. Well, I hope—and Mr. Davis, your view?

Mr. DAVIS. Yes, we have not been contacted by them for our input.

Mr. WILSON. Well, I certainly know what a resource you can be. And so I hope that you would be contacted, and I know how broad-based both of your organizations are. And I pay dues to ROA [Reserve Officers of America] and some others, too. So, American Legion comes to mind, VFW [Veterans of Foreign Wars]. So, retiree organizations, active. And I would just note that they would give heartfelt, real-world examples first-hand of the consequence of any reform effort.

I would like to proceed to Mr. Coffman.

Mr. COFFMAN. Thank you, Mr. Chairman.

I was in the military, in the Army, on Active Duty during the first, well, reduction in force that I can remember, which was in the early 1970s, post-Vietnam.

Now, fortunately, I don't—there was no separation pay as was in the early 1990s post-Gulf War and that reduction in force, where I think they gave a lump sum payment to separating, I think, senior noncommissioned officers and officers who were forced out in that process.

And I think that what is stressful for that population in a reduction in force is that there is no understanding of what the system is going to be until they receive notice that they are going to be out. Then there may be a decision that will help them, and there may not, and that is unfortunate.

And I think that is one reason why I think it is important to have a reform that reflects some accrued retirement benefit for people less than 20 years. And I think that is something that it is important to look at, watch out for. And certainly I want to reiterate again that I think that whatever system we put in place should not impact the people currently on Active Duty.

With that, Mr. Chairman, unless there are any responses from the panel to what I just said?

Mr. STROBRIDGE. I would just comment, sir, that the separation pays that you are talking about, at least as far as the law is concerned, those are deemed—we don't think that is right, but when you look at the law, it is hard to come to any conclusion that it is deemed a kind of retired pay payment.

If you take that and then come back in the service and qualify for retirement, they are going to deduct that separation pay from your retired pay.

So we don't like that, but that is the way it is. In other words, under current law, that is the retired pay outlay, the separation pay.

Mr. COFFMAN. Just one final point, and that is, on Active Duty in the Army and the Marine Corps, I served in combat arms, except for my last tour in Iraq was civil affairs. But, Gulf War, I was a light-armed infantry military officer, and then I was mechanized infantry in the United States Army.

And I got to tell you that that pretty much wore me out. And I think, to the casual observer, they will verify that, that there is

such a wide disparity in occupations in the military. And I got to tell you, there are a lot of them that people show up to work in the morning and leave in the afternoon, and it is not a whole lot different than, quite frankly, than a civilian job.

And there are those jobs that are just tough. And I believe that, if we can't recognize that in retirement, we ought to recognize it in plussing up hazardous duty pay, plussing up sea duty pay and all those other things that recognize people that don't punch out on Saturday, on Friday afternoon and go home, and just, you know, go day after day after day.

And I have done that in theater, in war, twice. And it is tough stuff. And so I think we need to recognize that. Certainly, I appreciate everybody who serves in the United States military, but I also appreciate that there are differences.

And with that, Mr. Chairman, I yield back.

Mr. WILSON. Thank you very much.

And, Congressman Heck?

Dr. HECK. No further questions.

Mr. WILSON. No further questions?

And, Colonel West?

Mr. WEST. No further questions.

Mr. WILSON. My goodness, Colonel. And Congressman Scott of Georgia?

Mr. SCOTT. No further questions.

Mr. WILSON. Mrs. Davis, any further?

There being no further, thank all of you for being here. You could tell the high interest and appreciation for your service. And again, military families—what we are talking about are consequences far beyond today, and we are looking for a very strong and positive future.

The meeting is adjourned.

[Whereupon, at 2:24 p.m., the subcommittee was adjourned.]

A P P E N D I X

OCTOBER 25, 2011

PREPARED STATEMENTS SUBMITTED FOR THE RECORD

OCTOBER 25, 2011

Statement of Hon. Joe Wilson
Chairman, House Subcommittee on Military Personnel
Hearing on
Military Retirement Reform
October 25, 2011

Today the Military Personnel Subcommittee will address the subject of military retirement, an issue of immense importance to service members and, in turn, to combat readiness.

I want to thank Dr. Joe Heck for recommending that the Subcommittee conduct this hearing. Dr. Heck very astutely recognized that military retirement would be a pivotal issue in the coming months and that it was essential that Subcommittee address the issue expeditiously. Thank you, Dr. Heck, for your insight and call to action.

The Defense Business Board, one element of the Department of Defense, was quick to present a major retirement reform proposal that set the tone of the retirement reform debate. The Board's proposal would move the retirement system aggressively toward a private sector defined contribution system based on the personal investments of service members. The proposal received immediate criticism from service members and military associations. The proposal is certainly a radical solution that would result in a significant reduction to retired benefits for all service members. As could be anticipated, the unveiling of the Defense Business Board proposal injected considerable uncertainty into the force, to include troops fighting the wars in Iraq and Afghanistan. The proposal created an immediate morale firestorm as service members feared that senior leaders within the Department of Defense and the military departments were seriously considering its implementation.

We invited the Defense Business Board to testify today to face the arguments of their critics and explain the merits of their proposal, but they declined the invitation. I am concerned that the Defense Business Board knowingly elected to pursue a very controversial proposal with immediate negative consequences for morale and combat readiness and yet they were unwilling to come before the Subcommittee and defend their action. In my view, their failure to appear speaks volumes about their own lack of conviction that their proposal is deserving of serious consideration.

Secretary of Defense Leon Panetta has been clear that retirement reform must be on the table for consideration as the Department of Defense contemplates the wide array of programs that will be considered for cuts to meet the budget reduction goals. I was pleased that the Secretary understood the morale problem that had been created by the Defense Business Board and announced his

clean support for grandfathering the benefits to be provided to currently serving members who have borne the burden of war over the last 10 years. We simply cannot betray the trust of the service members who have performed with such courage and expertise in Afghanistan and Iraq.

I was disappointed that Secretary Panetta did not disavow the Defense Business Board proposal. That statement would have removed a major irritant to the force. I was, however, very pleased at General Dempsey's statement before the House Armed Services Committee that recognized the unique requirements of military service and that strongly asserted that the military requires a retirement system totally different from any civilian retirement program.

Today, we hope to learn more about the current positions of the Department of Defense and military advocacy groups concerning the need to reform military retirement.

Statement of Hon. Susan A. Davis
Ranking Member, House Subcommittee on Military
Personnel
Hearing on
Military Retirement Reform
October 25, 2011

Given the current state of our Nation's economy, discussions on the condition and future of military retirement are once again being raised. Such discussions are not new, during previous economic down turns, focus has turned to the sustainability and affordability of our military retirement program. However, for the most part, the current military retirement program was established over 60 years ago, so it is valid to ask ourselves is this program as it currently exists still meeting the requirements it was set up to achieve, which is the focus of today's hearing.

Only 17 percent of the force actually completes a full 20 years of service in order to qualify for a non-disability retirement. Many have expressed concerns that the current program does not recognize the sacrifices of those who served during 10 years of conflict and may not stay the full 20 years to earn a retirement. Is it fair that that person who may have been deployed once, and stays to retirement, is eligible for a lifetime benefit, while an individual who may have multiple deployments in a combat theater, but does not stay 20 years, walks away with nothing more than the admiration of a grateful nation?

When the 20-year retirement program was established the life expectancy in 1949 for a white male was 66.2 years, for a black male it was 58.9 years. Compared to the latest data available, the life expectancy in 2009 for a white male is 76.2 years, and for a black male it is 70.9 years. There is no doubt that Americans are living longer and more fuller lives, which means that an average individual who receives military retirement for 20 years of service will receive retirement for nearly twice as long in her or his adult life. In addition, many of those who retire at 20 years of service have gone on with an ability to seek another full career in a different field.

Changes to the personnel compensation programs, including the retirement system, often strike fear in the force, so it is important that we do not unnecessarily undermine the faith of those who are currently serving. But, we do have a responsibility to ensure that the compensation package that is provided to service members is meeting the needs of our Nation's national security, and that includes looking at the military retirement package.

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Prepared Statement

of

The Honorable Jo Ann Rooney

**Principal Deputy Under Secretary of Defense for Personnel and
Readiness**

Before the

House Armed Services Military Personnel Subcommittee

October 25, 2011

Chairman Wilson, Congressman Davis and distinguished members of the subcommittee, thank you for the opportunity to come before you on behalf of the men and women who so ably serve in the uniforms of our nation's armed forces.

I am here today to speak to you about the state of the military retirement system for our uniformed services. Since the military transitioned to an All Volunteer Force, military compensation has been under continuous scrutiny. The primary goals of the military compensation system are to attract, retain, distribute, and eventually separate members so the U.S. can field a force to deter potential enemies, and when called upon, succeed on the battlefield. Even though some consider military benefits significant, we must remain cognizant that they support the brave men and women who volunteer to defend this great nation.

These men and women are a very small portion of our population, and they bear significant burdens on behalf of our nation. They endure substantial physical risks and many have deployed multiple times. They uproot their families frequently in support of our national defense. Our nation places great demands on them and has great expectations of them. Our recognition and remuneration of them should be equally significant and should acknowledge their continued sacrifices. Some believe the military retirement system is rich and generous when compared to the private sector. While compensation should be in line with the private sector, it should not be the same. The sacrifices these men and women bear are very different and these differences should be reflected in their compensation.

Today's military retirement system was created in an earlier era, long before the advent of the All Volunteer Force. The retirement system for active duty members is a defined benefit plan that is based upon years of service (YOS) and the basic pay earned near the end of the member's career. To qualify for regular retirement, the member must complete at least 20 years

of active duty or equivalent service. This is referred to as cliff vesting at 20 years. The monthly retired pay begins immediately after retirement and is a lifetime entitlement. The reserve components and National Guard have a related but somewhat different retirement system.

In general, the military retirement system accomplishes the purpose for which it was designed. The 20-year cliff vesting schedule provides a strong incentive to attain 20 years of service, especially for those who have served at least 10 years. After completing 20 years of service the incentive is to leave active duty shortly thereafter.

The current military retirement system has a number of advantages. It is generally well understood, predictable, and robust. It also influences retention behaviors across the force in a manner that varies little from year to year, allowing force managers to forecast accurately and ensure each Service retains sufficient manpower by strength, skill, and specialty.

A number of criticisms, however, have also been leveled at the current military retirement system. Some have argued that the current system defers too much of military compensation until later years and that more of this deferred compensation should be placed in current cash compensation. Others complain that because vesting in the current system does not occur until a member has served 20 years, only a fraction of the force receives any retirement benefit; in fact, most leave with no retirement benefits. Despite these criticisms, the current military retirement system has served the Department well. Over time, however, while the military retirement system has remained essentially the same, the world and private-sector compensation practices have changed.

At the time the Department transitioned from the draft to the All Volunteer Force, private sector employees often remained with one employer for an entire career. Defined benefit

retirement plans with cliff vesting schedules were common and retirement benefits were not as portable as they are today.

Over time, the demographics of the workforce have changed. Unlike their predecessors, the generation entering the workforce today expects to work for many employers over the course of a career. Life expectancies have increased, and second or multiple careers have become the norm. Private sector retirement plans have changed to more closely align with the changing workforce. Today, portable, defined contribution plans, such as 401(k) plans, are the norm, and defined benefit retirement plans with cliff vesting have become much less common.

Companies in the private sector have adjusted and reacted to these changes, with many routinely hiring employees in the mid and senior levels from outside the company workforce. While the Department has some flexibility in this area, the services must grow most of their military workforce internally. It generally takes 15 to 20 years to develop the next generation of infantry battalion commanders and submarine captains. As a result, the Department must ensure military compensation, promotions, and personnel policies all foster greater retention and longer careers necessary to create these experienced leaders. This need for greater longevity and continuity suggests there are valid reasons why mirroring a private sector compensation package may not necessarily be the proper approach for the military.

The Department recognizes the generous funding and support the Congress has provided to sustain our military, especially over the past decade in which the country has been at war. However, the Department also recognizes the importance and urgency of addressing the prolonged economic downturn and the country's current fiscal situation. As such, the Department expects to do its part.

Over the past year, the Department has begun reviewing the military retirement system in order to identify possible changes or alternative systems. The officer, enlisted, and civilian leadership of all Services, from the active duty, reserve, and National Guard components as well as the United States Coast Guard are participating. The review is designed to be deliberate, careful, and pragmatic. The Defense Business Board proposal is one of several proposals that are being reviewed and modeled to determine the impact on recruiting and retention. The Department is working to strike the right balance, weighing the impact of a new system on recruiting and retention, considering the welfare of the individual service member and family and, acknowledging our responsibilities to the American taxpayer.

As history has shown, changing the military retirement system is difficult, and the impacts of the changes are often only felt many years after the change. As this Congress knows, the changes to the military retirement system in the mid-1980s to the REDUX military retirement system, required rethinking after problems with retention surfaced 10-15 years after implementation. The Department is determined to avoid the same delayed impacts felt following the changes to the REDUX system, if changes are made to the current retirement system.

Before proposing changes to the military retirement system or any part of the military pay and benefits structure, however, the Department is committed to conducting significant evaluation and in-depth analysis of any proposal. The Department must ensure its ability to continue recruiting and retaining the highest quality All Volunteer Force. The Department needs to ensure any proposed changes do not break faith with current members and must also understand, to the fullest extent possible, the impact of any changes on the future of our All Volunteer Force.

At this time, the Department does not have any specific proposals or recommendations ready to offer. Within the last month, the President recommended forming a Commission to review the military retirement system. , The Department expects to provide significant input to the Commission, and also expects that any proposals offered will similarly be presented to the Congress and to this subcommittee for discussion and evaluation. I look forward to continuing to work with each of you as the Department moves forward on this issue. I thank you again for the opportunity to testify and for your continued support of our military members and their families. I look forward to your questions.



T H E M I L I T A R Y C O A L I T I O N

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STATEMENT OF
THE MILITARY COALITION (TMC)

before the

Subcommittee on Military Personnel

House Committee on Armed Services

on

The Uniformed Services Retirement System

October 25, 2011

Presented by

Steve Strobbridge, Colonel, USAF (Ret)
Director, Government Relations
Military Officers Association of America
Co-Chairman, The Military Coalition

John Davis
Legislative Director
Fleet Reserve Association
Co-Chairman, The Military Coalition Retired Affairs Committee

MISTER CHAIRMAN AND DISTINGUISHED MEMBERS OF THE SUBCOMMITTEE. On behalf of The Military Coalition, a consortium of nationally prominent uniformed services and veterans' organizations, we are grateful to the Subcommittee for this opportunity to express our views concerning the uniformed services retirement system. This testimony provides the collective views of the following military and veterans' organizations, which represent approximately 5.5 million current and former members of the seven uniformed services, plus their families and survivors.

- Air Force Association
- Air Force Sergeants Association
- Air Force Women Officers Associated
- AMVETS (American Veterans)
- Army Aviation Association of America
- Association of Military Surgeons of the United States
- Association of the United States Army
- Association of the United States Navy
- Chief Warrant Officer and Warrant Officer Association, U.S. Coast Guard
- Commissioned Officers Association of the U.S. Public Health Service, Inc.
- Enlisted Association of the National Guard of the United States
- Fleet Reserve Association
- Gold Star Wives of America, Inc.
- Jewish War Veterans of the United States of America
- Iraq and Afghanistan Veterans of America
- Marine Corps League
- Marine Corps Reserve Association
- Military Chaplains Association of the United States of America
- Military Officers Association of America
- Military Order of the Purple Heart
- National Association for Uniformed Services
- National Guard Association of the United States
- National Military Family Association
- Naval Enlisted Reserve Association
- Non Commissioned Officers Association
- Reserve Enlisted Association
- Reserve Officers Association
- The Retired Enlisted Association
- Society of Medical Consultants to the Armed Forces
- United States Army Warrant Officers Association
- United States Coast Guard Chief Petty Officers Association
- Veterans of Foreign Wars of the United States
- Vietnam Veterans of America
- Wounded Warrior Project

The Military Coalition, Inc., does not receive any grants or contracts from the federal government.

Overview

Mr. Chairman and distinguished members of the Subcommittee, The Military Coalition (TMC) thanks you for your continued, unwavering support for the fair treatment of active duty, Guard, Reserve and retired members of the uniformed services, and their families and survivors.

Over the past 11 years and more, this Subcommittee has been the primary champion of ensuring that the sacrifices of the career force are adequately recognized in their compensation package.

When the pay and benefit cutbacks of the 1980s and 1990s undermined retention and readiness, it was this subcommittee that worked to restore pay comparability, repeal unwise retirement “reform” cutbacks, restore military health coverage for older beneficiaries and correct longstanding compensation penalties imposed on disabled retirees and survivors.

You and the Subcommittee staff, along with your Senate counterparts, are Congress’ institutional memory and its repository of expertise on the close relationship between compensation, retention and readiness and what can go wrong when that relationship gets out of balance.

You have shepherded the all-volunteer force successfully through previous times of fiscal austerity and through times of protracted war.

Now, when that force has been through a decade of arduous wartime sacrifice never envisioned by its architects and when the Nation again faces a period of extraordinary fiscal challenges, the Coalition looks to you again to exert a leadership role in ensuring the lessons of the past are not forgotten and the that Nation will continue to fulfill its reciprocal obligation to those who serve a career in uniform protecting its vital interests.

The Coalition is particularly concerned that many in the Administration and some in Congress appear unaware of the history of adverse outcomes associated with past compensation cutbacks, and views these vital programs simply as sources of savings, without adequate regard to the impact of such changes on long-term readiness.

The Coalition believes strongly that significant changes in the crucial career incentives that form the core pillars of the all-volunteer force must be approached with considerable care and skepticism, considering repeated experience with past, ill-advised adjustments that ended up costing the country at least as much to fix as they had been projected to save.

The Military Retirement System

There are three separate retirement programs for the uniformed services – final basic pay, high-36-month average basic pay, and REDUX.

Most current retirees retired under the final basic pay system, which provides 2.5% of final basic pay per year of service (e.g., 50% of basic pay after 20 years), with annual cost-of-living adjustments (COLAs) tied to the rise in the Consumer Price Index during the previous year (the same COLA system used for Social Security).

Members who entered service after Sept 8, 1980 have their retired pay based on 2.5% of their highest 36 months' average basic pay per year of service, also with annual CPI-based COLAs. The vast majority of currently serving personnel serve under this system. This system yields about 8% less lifetime retired pay value than the final basic pay system.

The REDUX system was enacted in 1986 and was applied to service entrants on or after Aug 1, 1986. It provides 2.5% times high-36-month basic pay per year of service, except that 1% is subtracted for each year of service less than 30 (e.g., 40% of high-36-months basic pay after 20 years of service). Further, REDUX retiree COLAs are adjusted annually at a rate 1% less than the CPI (CPI-1). Under the REDUX law, retired pay is recomputed on a one-time basis when the retired member attains age 62. At that point, retired pay is recomputed to the amount that would have been payable under the high-36-month average system. After age 62, CPI-1% COLAs continue for life. The REDUX system further reduced lifetime retired pay value by up to 27%.

Congress repealed REDUX as the default system for post-1986 entrants in 2000 after the Joint Chiefs of Staff complained that it was undermining career retention and readiness. At the time, the REDUX system was the most frequently mentioned specific reason for leaving service among separating personnel.

Under current law, the high-36-month retired pay system is the default option, but servicemembers have the option at the 15-year point of electing the REDUX option in return for a one-time \$30,000 taxable career retention bonus. Only a minority of servicemembers choose this option, and the Coalition believes strongly that accepting this option is a very unwise decision.

Replacement Value of Retired Pay

Many wrongly believe that uniformed servicemembers receive "50% of pay after 20 years of service," but that is not the reality. The retired pay calculation is based solely on basic pay. Unlike civilians whose retirement is based on their full salary (often including locality differentials), the servicemember's housing and subsistence allowances are excluded from the retired pay calculation.

Thus, a servicemember with 20 years of service earns a retired pay amount that replaces approximately 34%-37% of his or her gross active-duty cash pay and allowances.

Purpose of the Uniformed Services Retirement System

The entire military compensation system, to include the retirement benefit, is based on certain underlying principles as outlined in the Department of Defense's (DoD) *Military Compensation Background Papers* and "should be designed to foster and maintain the concept of the profession of arms as a dignified, respected, sought after, and honorable career."

The whole purpose of the unique military retirement and healthcare package is to offset the extraordinary demands and sacrifices inherent in a service career. They were built to provide

a powerful incentive for top-quality people to serve 20-30 years in uniform, despite the burden of sacrifices eloquently articulated by the Secretary of the Air Force during his January 18, 1978 testimony before the President's Commission on Military Compensation:

“The military services are unique callings. The demands we place on our military men and women are unlike those of any other country. Our worldwide interests and commitments place heavy burdens and responsibilities on their shoulders. They must be prepared to live anywhere, fight anywhere, and maintain high morale and combat efficiency under frequently adverse and uncomfortable conditions. They are asked to undergo frequent exposure to risk, long hours, periodic relocation and family separation. They accept abridgement of freedom of speech, political and organizational activity, and control over living and working conditions. They are all part of the very personal price our military people pay.

“Yet all of this must be done in the light of – and in comparison to – a civilian sector that is considerably different. We ask military people to be highly disciplined when society places a heavy premium on individual freedom, to maintain a steady and acute sense of purpose when some in society question the value of our institutions and debate our national goals. In short, we ask them to surrender elements of their freedom in order to serve and defend a society that has the highest degree of liberty and independence in the world. And, I might add, a society with the highest standard of living and an unmatched quality of life.

“Implicit in this concept of military service must be long-term security and a system of institutional supports for the serviceman and his family which are beyond the level of compensation commonly offered in the private, industrial sector.”

There is no better illustration of that reality than the experience of the past decade, during which 1% of Americans has been made to bear the entire burden of wartime sacrifice for the other 99%. *Absent the career drawing power of the current 20-year retirement system and its promised benefits, the Coalition asserts that sustaining anything approaching needed retention rates over such an extended period of constant combat deployments would have been impossible.*

The crucial element to sustaining a high-quality, career military force is establishing a strong bond of reciprocal commitment between the servicemember and the government. If that reciprocity is not fulfilled, retention and readiness will inevitably suffer.

The Coalition believes the government has a unique employer's responsibility to the small segment of Americans it actively induces to serve for 20 to 30 years under all the conditions described above that goes far beyond any civilian employer's obligation to its employees.

Criticisms of the Retirement System

The uniformed services retirement system has had its critics since the 1970s and even earlier.

Budget pressures of the time led to implementation of the high-36-month average system and subsequently the REDUX system.

Both before and since, innumerable studies and task forces have recommended dramatic changes, usually either to save money, to make the system more like those offered under civilian programs, or both.

Most recently, groups such as the National Commission on Fiscal Responsibility and Reform, the Debt Reduction Task Force, the Sustainable Defense Task Force, and the Defense Business Board's "Modernizing the Military Retirement" Task Group have all recommended revamping it.

Outgoing Secretary of Defense Robert Gates was recently quoted as calling the military retirement system a "rigid, one-size-fits-all approach" and "unfair" because over 70 percent of those that enter military service don't make it to 20 years of service.

Alice Rivlin, former Director of the Office of Management and Budget (OMB) and founding director of the Congressional Budget Office (CBO), was appointed by the President to his National Commission on Fiscal Responsibility and Reform and also was a co-chair of The Debt Reduction Task Force.

Both groups' findings were critical of the existing retirement system calling it "inequitable" or "out of line with pensions in the private sector."

But what appears to be "new" is merely a repackaging of past criticisms.

For example, in January 1978, only a few years following the advent of the all-volunteer force, then CBO Director Alice Rivlin released a report named, "*The Military Retirement System: Options for Change*" intended as a basis for future debate with Congress and the Administration at the time. That report outlined the criticisms of the military retirement system at the time: again, "unfair" and "inflexible".

Other than the ill-fated REDUX effort, Congress has wisely ignored and dismissed these ivory-tower recommendations for very good reasons, which the Coalition wishes to examine more closely.

"Inflexibility": One frequent criticism of the existing retirement system is that it is inflexible and limits the ability of Service personnel managers to more precisely and effectively manage the force.

The Coalition strongly disagrees.

The Services already have substantial authority to adjust high-year-of-tenure limits to enforce the unique military "up-or-out" promotion system.

Other authorities exist, and services are currently exercising them, to incentivize voluntary separations and voluntary or mandatory early retirements.

Service managers routinely tighten retention and reenlistment incentives and restrictions when budget or other considerations create a need for additional separations and retirements.

When necessary, Congress has provided additional special drawdown authorities.

But the practical reality is that precisely planned force management initiatives are regularly tossed aside in the wake of world events that force dramatic reversals of those planned actions.

No force planner suspected on Sept. 10, 2001 that the Nation would be facing a decade of protracted war. And for the first several years of that conflict, Defense and service leaders actively resisted initiatives to grow the force to meet requirements for what they simultaneously acknowledged would be a “long war.”

The unfortunate reality is that the one thing history tells us about the Services’ best-laid plans for the future force is that they will likely be proven inappropriate for the world future force leaders will actually have to deal with.

Plans that envision delaying retirement eligibility until age 57 or 60 belie the reality that the services don’t want the vast majority of servicemembers to stay in uniform that long.

Some physically demanding career fields require young physically fit members. There is a reason that all services impose high-year-of-tenure limits for those whose future promotion appears unlikely.

And in keeping with the uncertainty of future plans mentioned above, the history of the force over the last several decades is that budget pressures regularly force mass early separations and retirements.

Service desires for unlimited flexibility to trim the force may be appropriate for management of hardware and other non-sentient resources. But the services are dependent upon attracting and retaining smart people who are capable of looking downstream and understanding all too well when their leaders put no limits on the sacrifices that may be demanded of them, but also wish to reserve the right to kick them out at will....even while building a system that assumes they will be willing to serve under these conditions until age 60.

Servicemembers from whom we demand so much deserve some stability of career expectations in return.

“Unfairness”: Another frequent criticism is that the current retirement system is “unfair” to those who choose to leave before attaining 20 years of service. They contrast this to the vesting requirement imposed on civilian retirement plans.

The Coalition sees both practical and philosophical flaws in this assertion.

First, as a practical matter, adding a vesting benefit would cost a significant amount of money, and neither the Administration nor Congress has indicated an eagerness to invest more money in the military retirement system.

Second, we have acknowledged that *there is a significant difference between service and civilian careers. The military has no lateral entry options available to civilian employers.* It is a promote-from-within system that requires much stronger inducements to complete a career in uniform.

Adding an early vesting option, by definition, can only detract from the pull to serve a full career. In times of poor retention, it would leave the government in the position of bidding against itself for their services.

Finally, virtually all vesting proposals would be paid for by subtracting a far greater sum from the retired pay value of those who serve a full career.

It's an odd concept of "fairness" that would significantly cut compensation value for those who serve longest under arduous military service conditions in order to provide extra compensation for those who choose to leave before completing career service.

The Coalition believes strongly that the retention power of the 20-year retirement system is the only reason the services were able to sustain retention and readiness in the face of the incredible wartime sacrifices imposed on servicemembers and families over the last decade.

Had the retirement reforms recently in the news been in effect during that period, the Coalition believes they would have destroyed career retention. If a 10-year servicemember is faced with a fourth deployment, with a choice between separating with a vested retirement or continuing to serve decades under these conditions, with retired pay delayed until age 60 – knowing that he or she almost certainly wouldn't be allowed to serve that long – what choice do you think most people would make?

The "fairness" issue for voluntary separatees is a red herring, because our first national priority must be fairness to those who complete an arduous, multi-decade career.

Recent Retirement Reform Proposals

Last month, the White House announced plan to establish a special commission to review the military retirement system, using a BRAC-like process under which:

- The Pentagon would develop a retirement reform proposal
- The DoD proposal would be referred to a special commission tasked with crafting a final proposal and subsequently forwarded to the White House
- If approved (without change) by the White House, the commission proposal would have to get an up-or-down vote by Congress, without any amendment options

The Coalition believes a BRAC-like "reform" process is particularly inappropriate for a program so crucial to sustaining long-term retention and readiness. A BRAC-like process limits debate, restricts the capacity for needed analysis and review, denies due-diligence review, and leaves this crucial program subject to the whims of a small group tasked to meet a deadline in a short time period.

The language in the Administration plan makes it clear that the intent of the initiative is to generate large savings by making the military retirement system more like civilian plans.

Such intent is inappropriate and shockingly insensitive to the radical difference between military and civilian working conditions. The last 10 years of war only emphasize that, if anything, military service conditions are even worse than they were when the current retirement system was enacted.

We believe that “civilianizing” the military benefit package would dramatically undermine the primary military career retention incentive and would be disastrous for retention and readiness, as they increase incentives to leave and reduce incentives for career service.

It is irresponsible to focus on budget and “civilian equity” concerns while ignoring the primary purpose of the retirement system – to ensure a strong and top-quality career force.

The White House plan comes on the heels of various studies, commissions, and task forces that have sought savings through various plans to reform the military retirement system.

For the most part, such proposals have envisioned requiring longer careers to earn an immediate annuity; changing the retired pay formula to yield lower initial pay; converting to a 401(k)-style system to shift more of the responsibility for retirement income to individual savings; reducing, delaying or means-testing annual cost-of-living adjustments; and imposing greater cost-sharing in military retirement health care.

Several specific proposals merit individual discussion.

Chained-CPI Cost-of-Living Adjustment (COLA): One of the most frequently mentioned options by most deficit-cutting panels is a “technical correction” to the Consumer Price Index (CPI) called the “chained CPI.”

Again, this isn’t a new idea. It’s been pushed for years by some economists who believe the CPI overstates inflation by failing to adequately recognize that consumers change their behavior when prices of some products and services rise sharply.

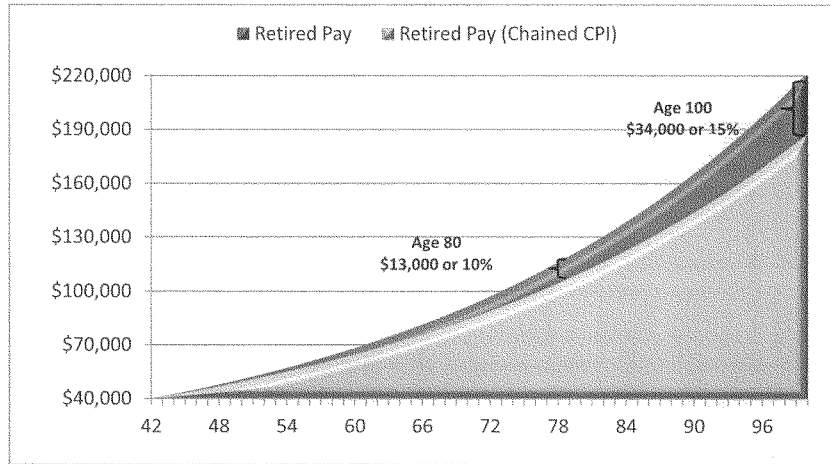
When that happens, economists say, people simply buy cheaper substitute products – chicken instead of beef when beef prices rise.

The case gets stickier with other substitutions. Is hamburger a reasonable substitute for steak? Is a compact car a reasonable substitute for a full-size one?

This is not just price substitution – it’s a quality-of-life substitution. Over time, this mentality leads to substantial changes in living patterns.

The Coalition believes that you need to look beyond the substitution philosophy to the bottom line. The chained CPI would reduce retired pay and other COLAs by about one-quarter of a

percentage point each year. That doesn't sound like much, until you see how that would compound over a retiree's lifetime (reflected in the following chart).



Military retirees and the disabled particularly would be affected because they start drawing inflation-adjusted pay at relatively younger ages. For a military retiree, switching to a chained CPI COLA would reduce total lifetime retired pay by about 6 percent. That's about \$100,000 for an E-7 retiring today with 20 years of service. A newly retiring O-5 with 20 years of service would lose double that amount.

And that's for someone living an average lifespan (early 80s). Half will live longer, and expected longevity is rising every year.

Three other factors are relevant here, as well.

First, the Bureau of Labor Statistics already made a change to allow some relatively modest substitutions several years ago.

Second, when COLA changes (delays) previously were proposed in the 1990s, the outcry from seniors successfully won an exemption for Social Security, leaving COLA penalties to fall disproportionately on military retirees.

Third, smaller COLAs aren't the only penalty of the chained CPI, because it also would be used for tax threshold adjustments. Smaller annual tax-bracket adjustments would lead to more people shifting into higher tax brackets every year.

For all of these reasons, the Coalition does not support the use of a chained CPI.

COLA Caps/Delays: During the budget-cutting years of the mid-1990s, several initiatives from various sources proposed artificially depressing annual military retired pay COLAs by .5% or 1% below the CPI, by means-testing COLAs to prevent their application to individuals above certain income levels, or to delay eligibility for COLAs until age 60 or longer.

The Coalition has ardently resisted COLA caps and delays as inappropriate for the uniformed services community.

First, they would defeat the purpose of inflation-adjusted COLAs, as stated in the words of historic House Armed Services Committee reports accompanying title 37, U.S.C.:

“(The COLA) reflects the progressive effort made by both the Executive Branch and the Congress to develop an automatic mechanism which would in the last analysis guarantee every military retired member that the purchasing power of the retired pay to which he was entitled at the time of retirement would not, at any time in the future, be eroded by subsequent increases in consumer prices.”

Arbitrarily capping COLAs at some percentage below the inflation measure used by the rest of the government would consciously condemn service retirees (many of whom are forced into early retirement by disability, service tenure limits and force cuts) to decades of continually eroding purchasing power. Compounded over time, they would dramatically cut retired pay value, and the effect would be greater the longer the retiree lived.

Similarly, means-testing retired pay COLAs would penalize most those who served longest and competed best in the services’ up-or-out environment. Implementing such a plan would create a perverse retention incentive.

Delaying COLAs until a later age would similarly undermine retention incentives and inordinately penalize those affected by disability and budget-driven force drawdowns. In the case of the latter group, it would impose an unfair and inappropriate double penalty.

Delaying COLAs until later in life would improperly penalize servicemembers for noncompliance with longevity requirements that are denied to the vast majority by law and service policies.

“High-5”: Another proposal suggested by some is to implement a “High-5” system under which retired pay would be based on the average of the highest 60 months (five years) of basic pay vs. the current “High-3” system that uses the highest 36 months’ average basic pay.

The net effect of this change would be to reduce retired pay by nearly 6% relative to the High-3 system, and more than that for members promoted within four years of leaving service.

The Coalition believes imposing a High-5 penalty would be inappropriate for the military because it would further discount and devalue the servicemember’s performance in his or her final grade.

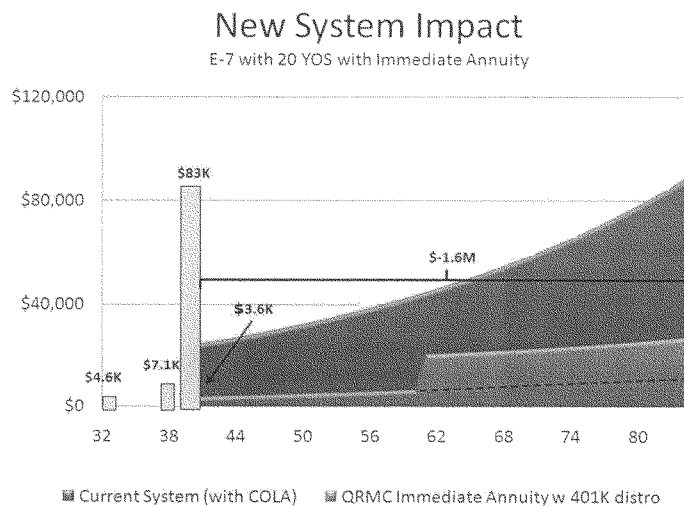
Under today's High-3 system, an E-7 retiring at 20 years of service receives retired pay of only \$23,900 – hardly a king's ransom.

A High-5 system would further reduce that to only \$22,600.

10th QRM Recommendation: Many recent proposals to “reform” military retirement have originated from the recommendations of the 2008 10th Quadrennial Review of Military Compensation's (QRM). The QRM proposed to:

- Convert the military to a civilian-style retirement system under which full retired pay wouldn't be paid until age 57-60
- Vest retirement benefits after 10 years of service
- Authorize the Services to pay flexible “gate pays” and separation pay at certain points of service to encourage continued service or encourage people to leave

The verbal description is one thing, but a graphic depiction is more insightful. First and foremost, it would drastically reduce retired pay annuities. The chart below compares the QRM proposal “immediate annuity upon retirement option” with that of the current retirement plan.



The red (darker) shaded area shows the current retired pay projection over time for a newly retiring E-7 at age 40 with 20 years of service. His/her retired pay of about \$24,000 a year would grow using a 3% COLA factor. This chart reflects the life expectancy (age 85) of 40-year-old E-7 newly retiring under the current system.

The QRM plan (blue [lighter] shaded area on the chart) would reduce retired pay 5% for each year before age 57 (17 years x 5% = 85% reduction), yielding only \$3,600 at age 40.

At age 60, the retiree would begin drawing money from a 401(K)-type plan. Using QRMC assumptions and projecting a 7% rate of return, the retiree would draw an additional \$13,600 per year until age 85. To be able to draw money beyond age 85, the annual withdrawal amount would have to be reduced.

To help entice people to serve longer, the QRMC envisioned a series of cash bonus payments (shown as three bars on the chart). The first two bars (\$4.6K and \$7.1K) reflect bonuses (before taxes) equal to 15% of annual basic pay at the 12 and 18 years of service points. In addition, the QRMC envisioned a separation bonus equal to a multiplier of 1 X monthly basic pay X years of service before taxes – 20 months of basic pay at 20 years of service.

But the bonuses wouldn't be guaranteed. The Services could turn them on or off depending on their needs in any particular year.

The bottom line is that the proposed system would reduce total expected lifetime retired pay for an E-7 with 20 years of service by a whopping \$1.6 million (and more than that for people who live beyond age 85), in return for taxable bonus payments of less than one-tenth that amount.

The Coalition believes the QRMC plan would do grave damage to long-term retention and readiness.

In effect, it would destroy most of the financial incentive to pursue an arduous military career particularly for enlisted members.

By dramatically reducing its financial commitments to servicemembers without any reduction in the enormous sacrifices demanded of career troops and families, it would invalidate any sense of reciprocal commitment between member and service.

The Defense Business Board Proposal: The QRMC plan is risky business. However, it pales in comparison when one considers the newest military retirement proposal briefed at the Defense Business Board (DBB) this past summer.

The Board's retirement task force recommended eliminating the current defined-benefit military retirement system and substituting a new 401(k)-like defined contribution plan with annual government contributions.

Many details of their recommendation are still undefined – such as how soon servicemembers would be vested and how much the government contribution would be.

Like the QRMC plan, the task force envisions leaving annual contribution amounts up to the Services, perhaps based on whether the servicemember was in a combat zone, on a hardship tour, or held a "higher risk" occupation. In addition, their plan would grandfather existing retirees and "fully disabled" veterans under the current system.

For currently serving personnel, they offered two options:

- A "high-cost" option would apply only to new service entrants, and grandfather all currently serving members under the current retirement system.

- A “lower-cost” option would immediately transfer all currently serving members to the new system, while crediting any time already served under the current system.

The latter option is what many civilian firms have done when changing retirement plans. Under this option, for example, a person who has 10 years of service upon implementation would get an annuity of 25% of high-three-year average basic pay upon retirement, whether he/she ended up serving 20 years or 30 years. But for the years after the implementation date, retirement credit would be built solely through the 401(k)-style system, with withdrawals allowed beginning at age 60.

This proposal would eliminate not only the defined benefit for retirees, but also the current Survivor Benefit Plan (SBP) for retiree survivors. Survivors would receive the “transportable” 401(k) in place of the current SBP annuity.

The Coalition is very concerned that shifting to a defined-contribution 401-(k)-style system would effectively void an important element of the government’s reciprocal obligation to those of whom it demands so much. There is no avoiding the risks of military service, up to and including death. But the uniformed services system has sought to offset that risk with assurances that survivors would be taken care of with a package of defined and predictable benefits, including an inflation-adjusted annuity that the survivor could not outlive.

The defined contribution system obviates that promise by requiring servicemembers and survivors to accept a large degree of financial risk over and above the normal risks inherent in a career of service.

The Coalition believes a defined, predictable retired pay and survivor annuity should remain a critical element of the military retirement package.

Let’s put the DBB’s proposal in perspective. The DBB is made up of corporate business leaders with limited military experience (only one retiree on the board) and is chartered to provide recommendations to SecDef – in this case, find ways to reduce costs of the current military retirement and provide something to those with less than 20 years of service.

The DBB talks of budget savings, but does not even mention the impact on future readiness or retention. This is serious. Not only would it put another strain on our servicemembers and their families because they would now face an uncertain future, it would threaten our national security, as many people are beginning to realize.

It is particularly galling to the Coalition that the DBB has characterized the existing retirement system as too rich a benefit for those who serve a long career and that it has “no comparison in the private sector.”

Few corporate employees face life and death decisions at work, or being shot at on a regular basis. Few have to leave their spouses to spend years in desolate, dangerous places while their families fend for themselves back home. They usually don’t have to move every year or two, to places they have no control over selecting and suffer the accompanying disruptions of spousal

careers and incomes and children's education. Bottom line – a military career has no comparison with a civilian career.

The DBB plan also would make it impossible for currently serving personnel to estimate their potential retired pay value as they decide whether to pursue a service career.

Under the current system, a servicemember can look at a pay table and have an idea what retired pay would be expected if they stay a specific period of time and attain a certain grade.

That would be impossible under the DBB plan, which would be subject to the vicissitudes of annual service budget cycles and the larger markets.

In sum, it adds a huge financial risk to all of the other risks inherent in a career of uniformed service. The Coalition believes that, of all Americans, those accepting the risks of a career in uniform deserve some reasonable certainty in terms of their expected reward.

Learning from the REDUX Lesson

Of all the reasons to be skeptical of dramatic retirement reform proposals, none is more cautionary than the very real experience with the REDUX system enacted August 1, 1986 that reduced 20-year retired pay value by approximately 25% for servicemembers who entered service on or after that date.

When Congress was considering the REDUX legislation, then-Secretary of Defense Casper Weinberger wrote congressional leaders to express his grave concern that the reduced career "pull" of lower retired pay compared to the continuing sacrifices inherent in a military career would eventually undermine retention (see attached Weinberger letter).

Those concerns proved justified in the 1990s, as surveys of separating servicemembers highlighted the REDUX system as a significant reason for their decisions to leave service. Subsequently, Congress repealed the REDUX system at the urging of the Joint Chiefs of Staff on readiness grounds.

Virtually all of the retirement reform proposals in recent years would impose far more draconian retired pay cuts on career service personnel than the REDUX law did.

If REDUX undermined retention and readiness in the peacetime years of the mid- and late 1990s and had to be repealed, how can we expect that far more severe cuts won't do much greater damage, especially in a wartime environment? Even if the current war were to end tomorrow, hard experience tells us any new service entrant can expect to spend some years at war.

The Coalition is dismayed that, in contrast to the prescient concerns of Secretary Weinberger for the future readiness consequences of the 1986 REDUX change, no current Defense or Administration leaders are voicing any such concerns about far more draconian changes.

The Coalition believes it is grossly irresponsible to ignore the obvious lessons of history in order to pursue ill-advised efforts to treat crucial retention and readiness programs as little more than a cash cow to achieve defense budget savings.

The Self-Deception of “Grandfathering” Against Ill-Advised Changes

Finally, the REDUX experience taught that grandfathering the current force against significant changes does not avoid the negative retention and readiness consequences of those changes.

Grandfathering is designed simply to quell dissent and fear among the currently serving, as there is no constituency for future entrants.

In the end, troops and families affected by such decisions have little or no say in what Congress and the Administration decide about their future compensation package. Their only recourse is to “vote with their feet” – as they did in the 1970s and 1990s – when they believe erosion of their career compensation package has left it insufficient to offset the sacrifices of continued service.

The REDUX experience shows grandfathering doesn't allow the country to escape the consequences of unwise actions. It only delays those consequences and throws them in the laps of successor Administrations and Congresses to solve – at potentially greater cost than their enactment had hoped to save.

The bottom line is still the same whether the current force is grandfathered or not: such proposals assert a belief that career troops' and families' service and sacrifice isn't worth what we're paying them.

The Coalition believes strongly that it's no less egregious to devalue the service of future entrants than that of the currently serving.

Conclusion

The most powerful argument for the current uniformed services retirement system is that it has worked – and worked extraordinarily well at sustaining career retention through the extraordinary variety of conditions the nation and our military have encountered over the last 60 years.

Through multiple wars and budget-driven force build-ups and drawdowns, it has proven highly effective in accomplishing its intended purpose.

The hard reality of the world is that the extraordinarily arduous service conditions it was intended to offset have not changed. If anything, service conditions have been worse in recent years than at any time since the current system was created.

We've tried the "cut it to save money" and "grandfather the current force" route with REDUX, and proved that didn't work.

So the bottom line remains. Military service is unique and cannot be compared to civilian retirement programs. It's essential to maintain a strong career force to be able to defend the country's national security interests. Anything that works against that is a bad idea.

The recommended military retirement system changes that have surfaced appear purely budget-driven and fail to take into consideration what will happen to retention and impact the readiness of our Nation's military. Had these types of "reform" been in place for the past decade, they would have destroyed the career force.

Dramatically reducing financial commitments to career servicemembers and families without any reduction in the enormous sacrifices demanded of them would destroy all sense of reciprocal commitment between member and service.

The Coalition understands that all areas of the budget must be able to stand up to scrutiny in this difficult fiscal environment. All we ask is a fair review that takes into account both the intent of these crucial programs and the hard experiences with dramatic changes of the past.

For those who argue that military people must accept a fair burden of national financial sacrifice, the Coalition answers that the Nation owes career military people a fair accounting of the sacrifices already imposed on them, including not only those imposed while on active duty, but also those imposed in retirement.

In that regard, let us not ignore the average 8-10% loss of lifetime retired pay incurred by servicemembers who retired under depressed pay tables of the last three decades because of pay raise caps experienced almost every year under the budget cutbacks imposed during the 1980s and 1990s.

Thank you for the opportunity to present the Coalition's views on this important topic.

Attachment: SecDef Letter dated 15 Nov 1985



THE SECRETARY OF DEFENSE
WASHINGTON, THE DISTRICT OF COLUMBIA

15 NOV 1985

Honorable Thomas P. O'Neill, Jr.
Speaker of the House of
Representatives
Washington, D.C. 20515

Dear Mr. Speaker:

The enclosed report complies with the requirements of section 667 of the Defense Authorization Act for fiscal year 1986.

Included in the report are drafts of the two pieces of legislation that would change the military non-disability retirement system. Each would result in a reduction in military retirement accrual funding of \$2.9 billion in fiscal year 1986 as mandated by the Congress. This is a 16 percent reduction in military retired pay from the current system and is in addition to the 13 percent reduction that was imposed by the Congress in the high-three-year averaging adjustment in 1980.

Although the Department of Defense has prepared the draft legislation as required by the Congress, I want to make it absolutely clear that such action is not to be construed as support for either of the options for change. To the contrary, the Department of Defense is steadfastly opposed to the significant degradation in future combat readiness that would result from the changes required to achieve the mandated reduction. I am particularly concerned about the potential loss of mid-level officers, NCOs and Petty Officers who provide the first-line leadership and technical know-how so vital to the defense mission. Unless offsetting compensation is provided, our models conservatively indicate that our future manning levels in the 10 to 30 year portion of the force would drop below the dismal levels of the late 1970s when aviator shortages and shortfalls in Army NCO and Navy Petty Officer leadership seriously degraded our national security posture.

While the changes we have been required to submit technically affect only future entrants, we expect an insidious and immediate effect on the morale of the current force. No matter how the reduction is packaged, it communicates the same message, i.e., the perception that there is an erosion in support from the American people for the Service men and women whom we call upon to ensure our safety. It says in absolute terms that the unique, dangerous and vital sacrifices they routinely make are not worth the taxpayers' dollars they receive, which is not overly generous. I do not believe the majority of the American people support this view and ask that you consider this in your deliberations on this very crucial issue to our national security.

Sincerely,

Enclosure

Colonel Steve Strobbridge (USAF-Ret)

Director, Government Relations, Military Officers Association of America (MOAA); and
Co-Chairman, The Military Coalition

Steve Strobbridge, a native of Vermont, is a 1969 graduate from Syracuse University. Commissioned through ROTC, he was called to active duty in October 1969.

After several assignments as a personnel officer and commander in Texas, Thailand, and North Carolina, he was assigned to the Pentagon from 1977 to 1981 as a compensation and legislation analyst at Headquarters USAF. While in this position, he researched and developed legislation on military pay, health care, retirement and survivor benefits issues.

In 1981, he attended the Armed Forces Staff College in Norfolk, VA, en route to a January 1982 transfer to Ramstein AB, Germany. Following assignments as Chief, Officer Assignments and Assistant for Senior Officer Management at HQ, U.S. Air Forces in Europe, he was selected to attend the National War College at Fort McNair, DC in 1985.

Transferred to the Office of the Secretary of Defense upon graduation in June 1986, he served as Deputy Director and then as Director, Officer and Enlisted Personnel Management. In this position, he was responsible for establishing DoD policy on military personnel promotions, utilization, retention, separation and retirement.

In June 1989, he returned to Headquarters USAF as Chief of the Entitlements Division, assuming responsibility for Air Force policy on all matters involving pay and entitlements, including the military retirement system and survivor benefits, and all legislative matters affecting active and retired military members and families.

He retired from that position on January 1, 1994 to become MOAA's Deputy Director for Government Relations.

In March 2001, he was appointed as MOAA's Director of Government Relations and also was elected Co-Chairman of The Military Coalition, an influential consortium of 33 military and veterans associations.

John R. Davis

Director of Legislative Programs
Fleet Reserve Association

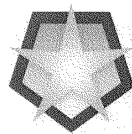
John Davis served in the United States Marine Corps Reserve in an artillery unit (155 self-propelled howitzers) and as a Second Lieutenant in the Illinois Army National Guard in the 1980s. He joined the FRA team as Director, Legislative Programs in February 2006, and recently stepped down as President of FRA Branch 181 (Arlington, Virginia) after serving two terms. He is co-chairman of The Military Coalition's (TMC) Retired Affairs Policy Committee.

John worked for almost 13 years with the National Federation of Independent Business, including 9 years as Director of the Illinois chapter and 3 ½ years in the federal lobbying office in Washington DC. John has lobbied on a variety of issues including healthcare, tort reform, education, insurance, taxation, and labor law.

In 2005 John received a Masters of Public Policy (MPP) degree from Regent University, Alexandria VA. He has a BS degree from Illinois State University in Political Science and History. John is a proud father of two children: Anne age 29 and Michael age 25 who returned from a 7 month deployment to Afghanistan (June 2010) with his Marine Corps Reserve unit.

DOCUMENTS SUBMITTED FOR THE RECORD

OCTOBER 25, 2011



DEFENSE BUSINESS BOARD

Report to the Secretary of Defense

**Modernizing the Military
Retirement System**

Report FY11-05

- **Recommendations to optimize the Department's military retirement system**
-

Defense Business Board

Modernizing the Military Retirement System**TASK**

The Secretary of Defense is committed to increasing the efficiency and effectiveness of the Department of Defense's (DoD) processes and operations. In May 2010, Secretary Gates tasked the Defense Business Board (herein referred to as "the Board") to review current Department policies and practices and identify options to materially reduce overhead and increase the efficiency of the Department's business operations (see **Tab A**). In response to this tasking, the Chairman of the Board established a Task Group to assess the military retirement system and develop potential alternatives that would enable the system to remain fiscally sustainable while recruiting and retaining the highest performing personnel required for our Nation's defense. A copy of the Terms of Reference outlining the scope and deliverables for the Task Group can be found at **Tab B**.

Mr. Richard Spencer served as the Task Group Chair. The other Task Group members were Patrick Gross, David Langstaff, Philip Odeen, Mark Ronald, Robert Stein, and Jack Zoeller. Catherine Whittington served as the Board Staff Analyst.

PROCESS

The Task Group conducted interviews with many of the Department's current senior leaders, former DoD and other government officials, several defense attachés from foreign ministries, and officials from institutes and government agencies. The Task Group also reviewed a multitude of analyses, studies, and recommendations generated by both government and private research institutions addressing military retirement over the past 30 years.

The Task Group's draft findings and recommendations were presented to the Board for deliberation at the July 21, 2011 quarterly Board meeting where the Board voted to approve the recommendations. See **Tab C** for a copy of the brief presented to the Board.

Defense Business Board

FINDINGS

The Task Group began by assessing the origins of the military retirement system and then compared it to the present environment. The current military retirement system has not been meaningfully modified or adjusted to reflect the creation of the All Volunteer Force. The system was designed in an era when life spans were shorter, draft era pay was substantially less than civilian sector pay, second careers were less common, and skills acquired during military service were not transferrable to the private sector.

The Task Group also compared the current military retirement system to various public, private, and foreign military systems. The Task Group observed that the present retirement system is tied to base pay and has therefore increased in direct proportion to the substantial increases in base pay that have occurred over the past ten years. As a result of these increases, today's regular military compensation is higher than that of average civilians with the same level of education. Enlisted and officer pay now ranks in the top quartile of all high school graduates and college graduates, respectively (see **Appendix A at Tab C**). As base pay increases, the size of the future retirement liability also increases.

The current system is based upon a 20 year cliff vesting structure. Those who serve less than 20 years receive no benefit, while those who serve for 20 years earn a lifetime benefit of 50 percent of base pay and those who serve for 35 years earn a lifetime benefit of 87.5 percent of base pay, all of which is regularly adjusted for inflation. For those serving more than 20 years, the retirement contribution is approximately 10 times greater than the private sector. Whereas average private sector pension contributions range from 4 to 12 percent per year, military retirement benefits equate to an approximate contribution of 75 percent of annual pay per year.

The Task Group identified three features of the current military retirement system that point to the need for change.

First, the current military retirement system is unfair. For example, 83 percent of those serving in the military will receive no retirement benefit. Military personnel serving 5, 10, or 15 years will depart from service with no

Defense Business Board

benefit or pension. This cohort includes the majority of troops who have engaged and will engage in combat. Conversely, only 17 percent of the All Volunteer Force serves for more than 20 years, and they are endowed with a lifetime benefit. The distribution varies between officer and enlisted personnel; 43 percent of officers and 13 percent of enlisted personnel have historically received a pension.

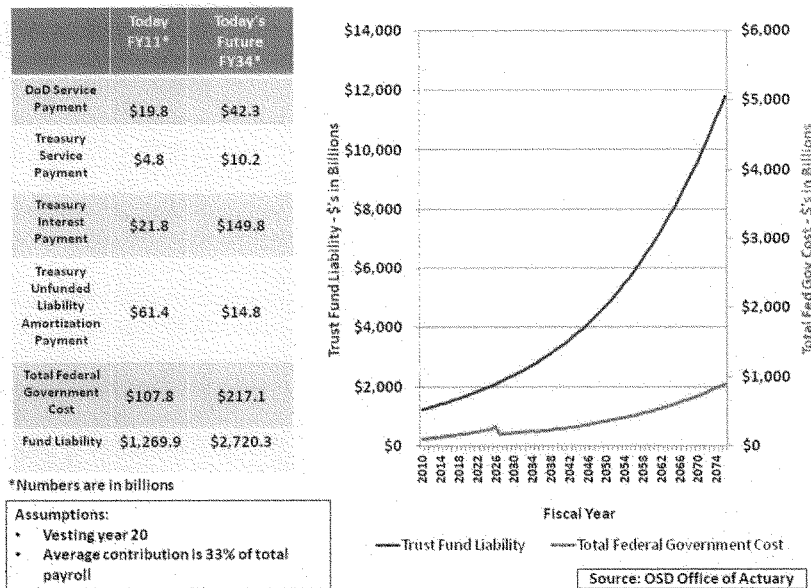
Second, the current military retirement system is inflexible and has disadvantages with regard to force shaping. The binary nature of the 20 year cliff vesting requirement creates a strong incentive for personnel to leave shortly after 20 years. Interviews indicated that, in some areas of specialization, military service members are only then reaching their peak performance at that point. Data from the Office of the Secretary of Defense (OSD) Office of Actuaries shows that with 20 year cliff vesting, 76 percent of personnel leave after serving between 20 and 25 years. At the same time, the cliff vesting requirement makes it more difficult to release personnel with 15 years or more of service. In periods of downsizing, as in the 1990s, the Department has therefore had to seek special payment authority to ease the transition out of the military.

Third, in light of the budget challenges DoD is currently facing, the military retirement system appears increasingly unaffordable. In FY11, the retirement plan will accrue 33 cents for each dollar of current pay, for a total of \$24 billion. As shown in the table and graph on page 4, these costs are rising at an increasingly unsustainable rate.

According to the OSD Office of the Actuary, annual military retirement payments are forecasted to increase from \$52.2 billion in 2011 to \$116.9 billion in 2035. As of today, the total life cycle program costs will grow from \$1.3 trillion, of which only \$385 billion is presently funded, to \$2.8 trillion by FY34 (see **Appendix D at Tab C**). Increases in inflation and life expectancy will further increase military retirement benefit costs. Moreover, as presently structured, any increase to base pay has an automatic and dramatic impact on future retirement liabilities.

Defense Business Board

Military Retirement Trust Fund Under Current Plan



RECOMMENDATIONS

The Board recognizes that retirement benefits are an important component of overall compensation. Other elements, such as current compensation, and other benefits (e.g. healthcare and education) constitute the broad compensation package. Any changes in military retirement should be considered in the context of the overall compensation package. The Board offers, as part of that process, the following recommendations to modify the military retirement system.

1. The Department should establish a new structure for the military retirement system, based on annual contributions. One model for this new structure is the existing Uniformed Military Personnel Thrift Savings Plan (TSP).

Defense Business Board

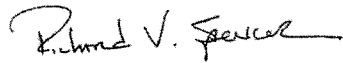
2. Contributions to the new plan would be made by the government. The amount of that contribution should be set at a rate to support retention in an ever changing global environment. For example, the government contribution could include an adjustment that would increase the contribution for longer serving military personnel to aid in retention. For modeling purposes only, the Task Group's analysis used an annual government contribution equivalent to 16 percent of military annual base pay – approximately two times the amount of annual contribution in the private sector. Investment options could also vary from 401(K) type plans to annuities or cash balance accounts.
3. Military members would also be able to make contributions to their own accounts. Furthermore, these retirement accounts would be transportable into the private sector and back into the military.
4. DoD contributions could vary depending on the needs of the services, such as larger contributions at certain retention gates, specific Military Occupational Specialty, or other demands to assist in force shaping.
5. The individual account would provide for rights of survivorship.
6. Fully disabled participants would qualify for an immediate pension, which would be formulated with VA benefits, as presently structured.
7. The plan would need to establish periods for initial vesting and for pay-out. One approach would be for a plan to begin vesting after the first recruitment period and become payable at ages 60 to 65 (or the Social Security age). The plan could allow for partial withdrawals or loans to cover education, healthcare, or other specified unplanned events or emergencies. Similar to most private sector severance plans, upon retirement, a time formulated transition payment option should be considered to facilitate the change to a new career.
8. This plan would apply to Reserve and Active Duty personnel. Retired and disabled personnel would be unaffected.

The Board recognizes the magnitude of the change involved in shifting to a different structure for the retirement system. One key option

Defense Business Board

for this change is a transition approach of which the Board made no specific recommendation. As input to decision-makers, the Board modeled two alternatives: the first which grandfathers all current military personnel in the existing system, and the second which involves a more rapid transition, but without loss of accrued benefits (see **Appendix E** and **F**, respectively, at **Tab C**).

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Richard V. Spencer". The signature is fluid and cursive, with a long horizontal stroke at the end.

Richard Spencer
Task Group Chair

TAB A

**SECRETARY OF DEFENSE
TERMS OF REFERENCE –
“REDUCING OVERHEAD AND IMPROVING BUSINESS
OPERATIONS”**



SECRETARY OF DEFENSE
1000 DEFENSE PENTAGON
WASHINGTON, DC 20301-1000

MAY 17 2010

MEMORANDUM FOR THE CHAIRMAN, DEFENSE BUSINESS BOARD (DBB)

SUBJECT: DBB Terms of Reference – “Reducing Overhead and Improving Business Operations”

I remain concerned over the ability of the Department of Defense to sustain current force structure levels and to continue critical modernization of military capabilities given the current and projected fiscal climate. For these reasons, it is imperative that the Department identify and pursue every opportunity to economize and increase the efficiency of its business operations.

As the Department's independent advisory board for economic and business affairs, I request you form a task group to provide recommendations on options to materially reduce overhead and increase the efficiency of the Department's business operations. This effort should identify both short- and long-term opportunities to achieve budget savings as well as make process or organizational changes that will yield long-term operational efficiencies.

The offices of Under Secretary of Defense (Comptroller), Cost Assessment and Program Evaluation, and Director of Administration and Management will serve as your principal support resource and will provide assistance as necessary. Other Department of Defense elements will provide assistance if determined to be necessary.

This effort should be completed by September 1, 2010, with an interim briefing to me by July 1, 2010.

A handwritten signature in dark ink, appearing to read "Robert M. Gates".



TAB B

**CHAIRMAN, DEFENSE BUSINESS BOARD
TERMS OF REFERENCE –
“MILITARY RETIREMENT–ALTERNATIVE PLANS”**



DEFENSE BUSINESS BOARD
1155 DEFENSE PENTAGON
WASHINGTON, DC 20301-1155

November 10, 2010

MEMORANDUM FOR RICHARD SPENCER

SUBJECT: Terms of Reference – "Military Retirement-Alternative Plans"

The Secretary of Defense is committed to increasing the efficiency of resource allocation within the Department of Defense in order to better align defense dollars with real-world military needs. In this ongoing environment of constrained resources, each component of the Department's budget must be reviewed to support the Secretary's goals. Therefore, a significant portion of the Department's personnel budget particularly, military pay and retirement should be appraised and benchmarked.

To support the Secretary's efficiency initiatives, I request you lead the Defense Business Board's "Military Retirement-Alternative Plans" Task Group. You should begin by reviewing the current reform thinking on military pay and benefits. This research and analysis will help you to provide recommendations for optimizing the Department's military pay and retirement system. Please provide recommendations that enable the system to be fiscally sustainable while recruiting and retaining the highest performing personnel required for our Nation's defense.

The Task Group will consist of you, Patrick Gross, Phil Odeen, Steve Reinemund, Mark Ronald, Robert Stein, and Jack Zoeller. Please provide me with your findings and any recommendations to improve our processes by the Defense Business Board's Quarterly Meeting in April 2011. Colonel Michael N. Pierce will serve as the Task Group's Military Assistant.

As a subcommittee of the Board, and pursuant to the Federal Advisory Committee Act of 1972, the Government in the Sunshine Act of 1976, and other appropriate federal regulations, this Task Group shall not work independently of the Board's charter and shall report its recommendations to the full Board's public deliberation. The Task Group does not have the authority to make decisions on behalf of the Board, nor can it report directly to any federal officer who is not also a Board member. The Task Group will avoid discussing "particular matters" according to Section 208 of Title 18, U.S. Code.



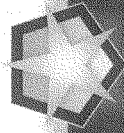
Michael J. Bayer
Chairman



TAB C

**FINDINGS AND RECOMMENDATIONS
PRESENTED TO THE BOARD
ON JULY 21, 2011**

DEFENSE BUSINESS BOARD



Modernizing the Military Retirement System

Task Group

July 21, 2011

Task Group Overview

Terms of Reference

In order to support the Secretary of Defense's efficiency initiatives, review the current structure and function of the military retirement system. Begin with a review of the current reform thinking on military retirement benefits. This research and analysis will help to provide recommendations for optimizing the Department's military retirement system.

Deliverables

Provide recommendations that will enable the system to be fiscally sustainable while recruiting and retaining the highest performing personnel required for our nation's defense.

Task Group Members

Richard Spencer (Chair)
Patrick Gross
David Langstaff
Philip Odeen
Mark Ronald
Robert Stein
Jack Zoeller

DBB Staff Analyst

Catherine Whittington

Methodology: Interviews

- **Current DoD**
 - Vice Chairman, Joint Chiefs of Staff (VCJCS)
 - Chief of Staff of the Air Force (CSAF)
 - Chief of Naval Operations (CNO)
 - Commandant of the Marine Corps (CMC)
 - Chief of Navy Reserve
 - Chief of Navy Personnel, DCNO, Manpower, Personnel, Training & Education, N1
 - Director, Plans and Resources, Office of the Deputy Chief of Staff of the Army, G1
 - Military Deputy for Budget, Office of the Assistant Secretary of the Army, Financial Management & Comptroller (ASA(F&MC))
 - Under Secretary of Defense for Personnel and Readiness (USD(P&R))
 - Director for Military Compensation (OUSD(P&R))
 - Joint Chiefs of Staff Working Group
 - Members who wrote the 11th Quadrennial Review of Military Compensation (QRMC)
- **Former DoD and Government Officials**
 - HON John Hamre
 - HON Ken Krieg
 - ADM Vern Clark, USN (Retired)
 - HON David M. Walker
 - HON Richard Danzig
- **Defense Ministries**
 - Canada
 - France
- **Institutes and Government Agencies**
 - Institute for Defense Analysis (IDA)
 - Congressional Budget Office (CBO)
 - Center for Strategic and International Studies (CSIS)
 - Center for Strategic and Budgetary Analysis (CSBA)
 - RAND Corporation
 - Office of Thrift Savings Plan
 - OSD Office of the Actuary

Where We Are Today

- The All Volunteer Force has proven to be an outstanding success
- Congress has shown consistent support for the military through increases in both compensation and benefits
- Military compensation is higher than that of average civilians with similar education levels (see **Appendix A**)
 - Enlisted pay ranks in the top quartile of that of high school graduates
 - Officer pay ranks in the top quartile of that of college graduates
- Retiree healthcare (TRICARE) is significantly more generous than civilian programs
- Military retirement exceeds levels in the private sector
- 83% of military personnel receive no retirement benefits

Findings

DoD has maintained the structure of its retirement benefits, which was created prior to the All Volunteer Force

- Retirement plans are an important component of both private and public sector compensation systems
- Over the last few decades, private sector plans have shifted from defined benefit to defined contribution to address longer life spans and unaffordable costs
- The military retirement system has not materially changed for over 100 years
 - The current military retirement system was designed for an era when life spans were shorter,
 - Pay was not competitive with civilian pay, and
 - Second careers were rare since military skills did not transition easily to the private sector
- Military retirement funds are not able to be invested in higher yielding equities and bonds

Findings (Continued)

Military retirement is more generous and expensive compared to the private sector

- DoD pays retirees 40 years of retirement benefits for 20 years of service
 - Military skills are transferrable to the private sector
 - Second careers are now common for those retiring in their 40s
 - Payout after 20 years makes retention difficult – 76% leave between years 20 and 25
 - 20 years of service earns a lifetime of payments of 50%, ramping up to 87.5% for 35 years of service
- Retirement funds accrued for personnel serving less than 20 years are effectively applied to the benefits of those serving more than 20 years
- For those serving more than 20 years, the retirement contribution is 10 times greater than the private sector
 - Average private sector pension contributions range from 4-12% per year; military retirement benefit equates to 75% of annual pay per year for those who retire
 - Immediate payout after 20 years has no comparison in the private sector

For FY11, total government contribution will be \$46B**

**Does not include \$64.1B in unfunded liability amortization payment

Findings (Continued)

“One Size Fits All” has structural disadvantages

- Surveys consistently report that military retirement has little value in recruitment or retention for at least the first 10 years of service
- The current plan is highly inflexible and especially poorly suited for periods of significant change (e.g., when downsizing the force)
 - It will be very difficult to release personnel with 15 or more years of service, yet these age groups are a probable target for downsizing
 - As a result, DoD will likely require special pay to ease transitioning out of the military (as was done in the 1990s), therefore, increasing costs
- The current system does not compensate for those in high risk situations or extenuating circumstances (e.g., combat duty, hardship tour, and separation from family)

Assessment

The Retirement Plan is Unfair

- The military retirement system lacks fairness in several dimensions.
 - Personnel serving 5, 10, even 15 years receive no retirement pay. Those serving 20+ years are endowed with a lifetime benefit.
 - The risky nature of military service is an important justification for the 20-year plan. However, most of the troops engaged in combat serve far less than the required 20 years. (Only 12%-13% of enlisted troops earn retirement pay).
- Retirement is a cost element attributable to each Service member, yet only 17% receive this benefit.
- There is no difference in retirement benefits between those who have served in high risk and low risk positions.

83% of those who serve will receive no retirement benefit

Assessment (Continued)

The Retirement Plan is Unaffordable

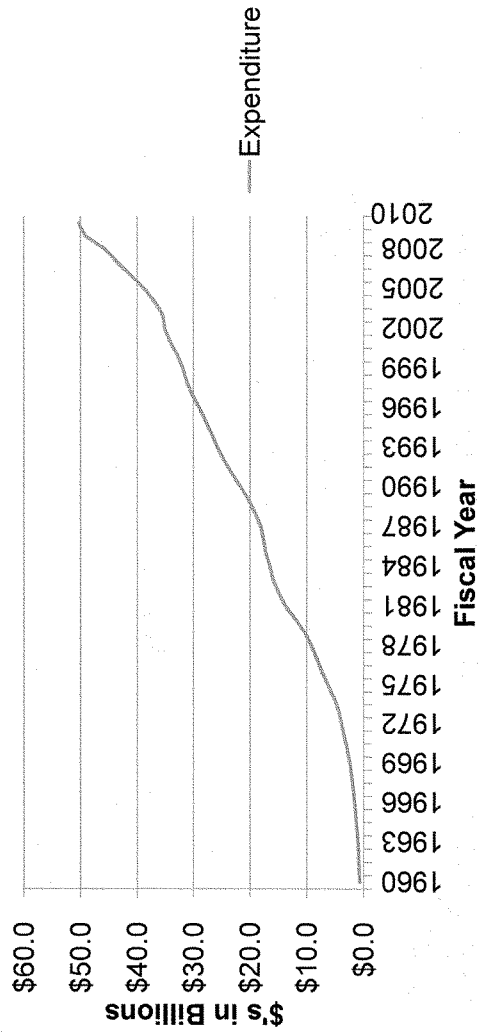
- The cost of military retirement will seriously undermine future military warfighting capabilities
- For each dollar of current pay, the retirement plan accrues 33 cents, for a total of \$24B** in FY11
- Costs are rising at an alarming rate; future liability will grow from \$1.3T (of which \$385B is funded) to \$2.7T by FY34
- Increases in inflation and life expectancy will further increase military retirement benefit costs
 - +1% inflation increase = \$3B military retirement benefit service cost increase
 - +1 year of life expectancy = \$300M military retirement benefit service cost increase

Action must be taken to contain these spiraling costs or they will undermine future warfighting capabilities

**Does not include Treasury interest of \$22B

Military Retirement Trust Fund Payments/Expenditures

Military Retirement Trust Fund Expenditures by Fiscal Year



Military retirement payments continue to increase (\$50B in 2010; \$108B in 2035)

Source: Valuation of the Military Retirement System, September 2009, OSD Office of the Actuary, Dec 10

Assessment (Continued)

The Retirement Plan is Inflexible

- The current system cliff vests at 20 years of active service
- Personnel with fewer years of service earn no retirement
- Only 7% of personnel leave between the 15th and 20th year of service, compared to 76% of those serving 20 to 25 years
- Years served is the only factor in the retirement benefit calculation, regardless of whether the Service member's career risk profile is in an administrative role or a high risk combat role
- Modifying the retirement system would create an effective force shaping tool

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Recommendation

A Comprehensive Solution: A New Defined Contribution Plan

- The most flexible and readily available plan would be based on the existing Uniformed Military Personnel Thrift Savings Plan (TSP), but with the government providing annual contributions (see **Appendix C**)
 - Payments into the plan would include an option for military member contributions
 - Plan accounts would be transportable into the private sector and back into the military
- DoD contributions could vary depending on circumstances, such as larger contributions for personnel at risk or on hardship tours
- The Defined Contribution Plan would provide flexibility to assist in force shaping and sizing
- The individual account would provide for rights of survivorship
- Fully disabled participants would qualify for an immediate pension formulated with VA benefits as presently structured

Key Elements of A New Defined Contribution Plan

- Establish a mandatory TSP program for all Military Service Personnel
 - The government contribution, including extra incentives, would be funded at a percentage level comparable to the highest end of a private sector pension plan
 - The plan would vest after 3 to 5 years, payable at age 60 to 65 (or Social Security age)
 - Partial withdrawals (or loans) to cover education, healthcare, or other specified emergencies
- Plan would be risk adjusted to recognize combat roles, family separation, and other unusual duty, for example:
 - Double contributions for years in combat zones or high risk positions
 - Greater contributions for hardship tours
 - Retirement age could be lowered using similar metrics
- Like most private sector severance plans, the option of a time formulated transition payment should be considered to facilitate the change to a new career
- Comprehensive solution would apply to Reserve as well as Active Duty personnel

The new plan would enhance fairness and flexibility, and provide a more affordable cost structure

Attributes of A New Defined Contribution Plan

■ Individual Features

- Uniformed Military Personnel TSP individual account
- Payout options to include: traditional payout, annuity, or lump sum
- Partial payout options to include: education, home ownership, or business acquisition
- Right of survivorship transferability upon death

■ Military Service Features

- Affordable, fair, and flexible solution to current system
- Risk profile multiplier and vesting option provides tool for force management either encouraging or discouraging retention
- Active Duty and Reserves under one plan

■ Coverage

- No impact on existing retired population
- Fully disabled veterans not effected by new plan

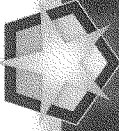
■ Transition Alternatives for All Present Active Duty Personnel

- Higher Cost Alternative – No transition (see **Appendix E**)
- Lower Cost Alternative – Immediate transition with no loss of accrued benefits (see **Appendix F**)

Conclusions

- The current military retirement system is out of date.
 - It is unfair, unaffordable, and inflexible.
 - As costs escalate, the continuation of the system will seriously erode future military capabilities.
- A comprehensive alternative that would fix these shortcomings is required.
 - All military personnel earn retirement benefits.
 - Costs are far more manageable in future years.
 - Contributions are flexible and reward longer service, high risk assignments, and family separation.
 - Retired and disabled members would be unaffected. They would still receive current benefits.
- Modifying the existing system to reduce cost would have to be dramatic to address affordability. The system would continue to be unfair and inflexible.
- Implementation should be phased-in to ensure current military personnel are treated fairly with due consideration to cost.

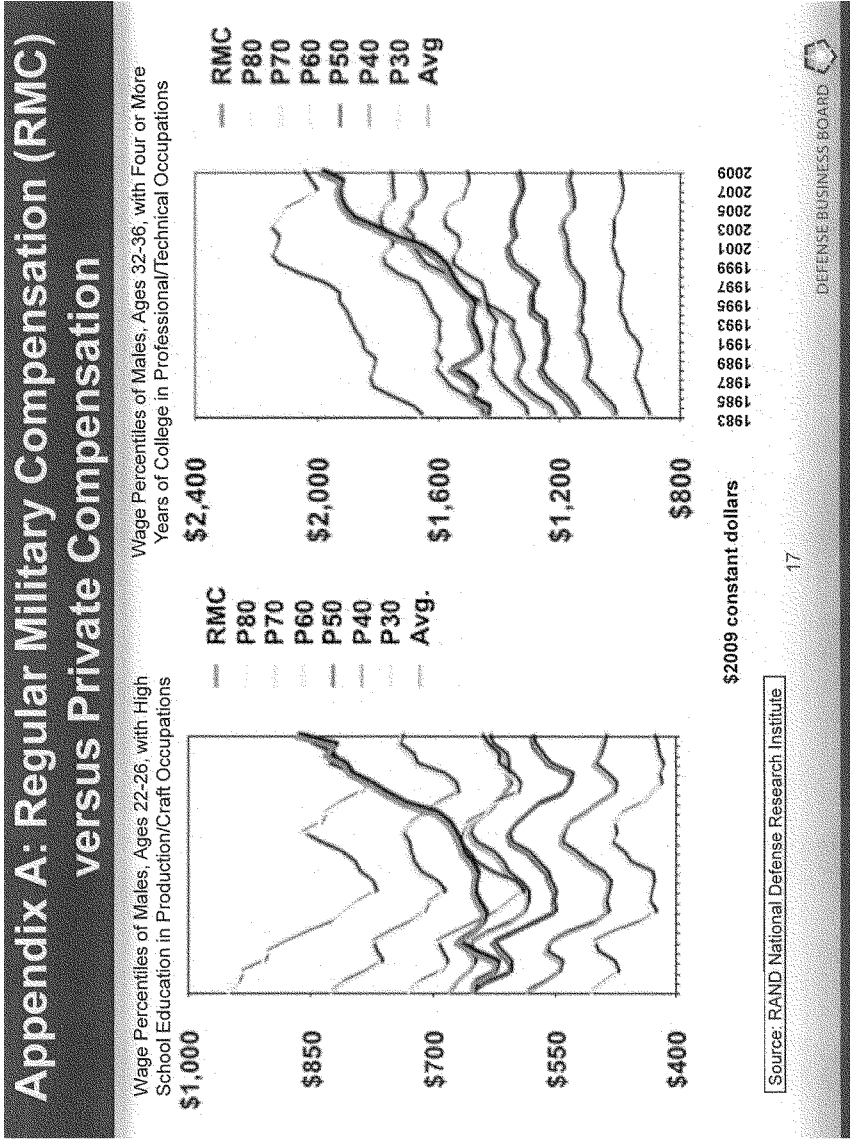
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Appendix B: Addressing Affordability of the Current System

- Amending the existing system for new entrants can have meaningful impact on sustainability while the volunteer force remains competitive with private markets
 - Index payout of retirement benefits to 67 years of age
 - Propose a one time Transition Payment paid at separation (e.g. one months salary for each year served)
 - Adjust benefit multiplier to 2.0 (40% of base Pay) from present 2.5 (50% Base Pay)
 - By comparison the following are averages of multipliers: private sector 1.1, public and municipal 1.5, and fire and police 2.0
 - Adjust High 3 computation to High 5
- These changes fail to address the inflexibility and unfairness of the current system

Cumulative Savings Over 20 Years

	Delay Pay	2.0 Multiplier	High 5	Total
FY32	\$193.3*	\$49.9*	\$10.9*	\$254.1*

40% cumulative savings by FY32

*Numbers are in billions

Source: OSD Office of Actuary

Appendix C: 2011 Uniformed Military Personnel Thrift Savings Plan

- \$16,500 annual tax-deferred contribution limit
 - Applies to Member contributions from basic, special, incentive and bonus pays
 - Does not include service matching contributions (for the few Service members receiving matching)
- \$5,500 annual tax-deferred “Catch-up” contribution
 - Applies to members who are (or will be) age 50 or older
 - Deducted from taxable basic pay, submitted as tax-deferred to the TSP
 - Catch-up contribution is in addition to the elective deferral and annual additions limit
- \$49,000 annual maximum contribution limit
 - Applies when member contributes while in a designated combat zone depositing tax-exempt contributions to the TSP (which accrue tax-deferred earnings)
 - Limit includes tax-deferred and tax-exempt member contributions from basic, special, incentive and bonus pays (but does not include catch-up contributions)
 - Limit applies to member contributions and any Service matching contributions received
 - Does not include amount contributed as catch-up during the year

Appendix D: Trust Fund Under Current Plan

	Today FY11*	Today's Future FY34*
DoD Service Payment	\$19.8	\$42.3
Treasury Service Payment	\$4.8	\$10.2
Treasury Interest Payment	\$21.8	\$149.8
Treasury Unfunded Liability Amortization Payment	\$61.4	\$14.8
Total Federal Government Cost	\$107.8	\$217.1
Fund Liability	\$1,269.9	\$2,720.3

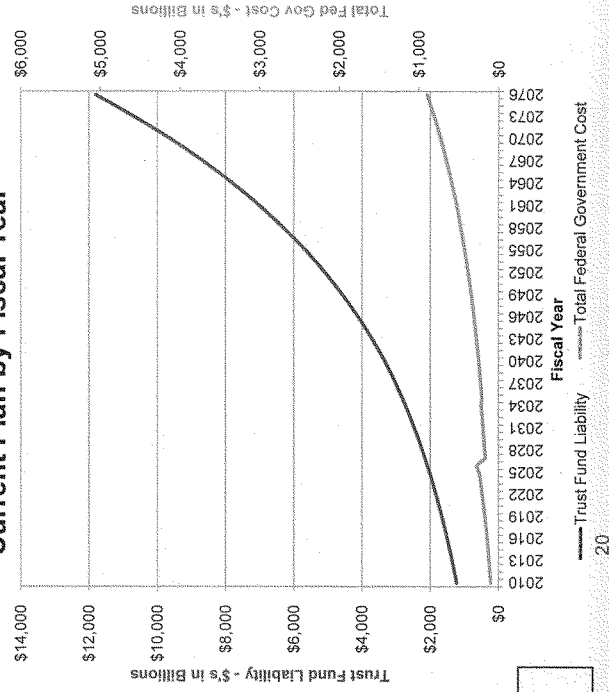
*Numbers are in billions

Assumptions:

- Vesting year 20
- Average contribution is 33% of total payroll

Source: OSD Office of Actuary

**Military Retirement Trust Fund Under
Current Plan by Fiscal Year**



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Appendix E: Trust Fund Under Revised Plan if All Current Active Duty Remain on Current Plan

	Today FY11*	Today's Future FY34*
DoD Service Payment	\$18.9	\$21.0
Treasury Service Payment	\$4.3	\$10.4
Treasury Interest Payment	\$21.7	\$100.7
Treasury Unfunded Liability Amortization Payment	\$61.4	\$14.8
Total Federal Government Cost	\$106.3	\$146.9
Fund Liability	\$1,266.7	\$1,800.0

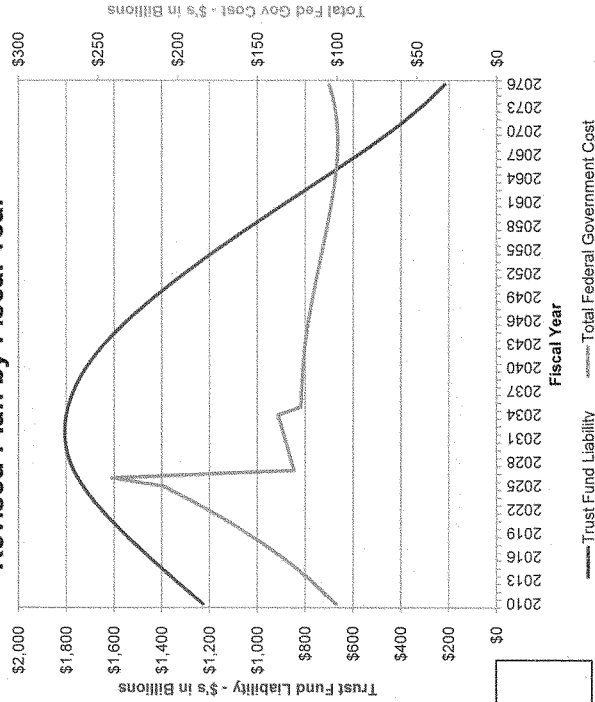
*Numbers are in billions

Assumptions:

- Average vesting year 4
- Active duty remains on current plan
- New recruits go on revised plan

Source: OSD Office of Actuary

Military Retirement Trust Fund Under Revised Plan by Fiscal Year



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Appendix F: Trust Fund Under Revised System if All Active Duty Personnel Transition Immediately

- Modeled after private sector approach and yields a viable lower cost alternative
- Rapid transition to new plan for total active force
- Preserve accrued benefit from “old plan” but no further accrual
- For those with less than 20 years – proportional benefit under “old plan” if they stay for 20+ years (example: 10 years of service would result in 10/20 of the old plan benefit at old vesting date or 25% of pay at retirement)
- All active duty personnel start to accrue new benefit for the balance of their service payable under new terms (age 65 nominal)
- Average DoD contribution under revised system includes all extra incentives (16.5% of total pay)

Appendix F: Trust Fund Under Revised System if All Active Duty Personnel Transition Immediately (Continued)

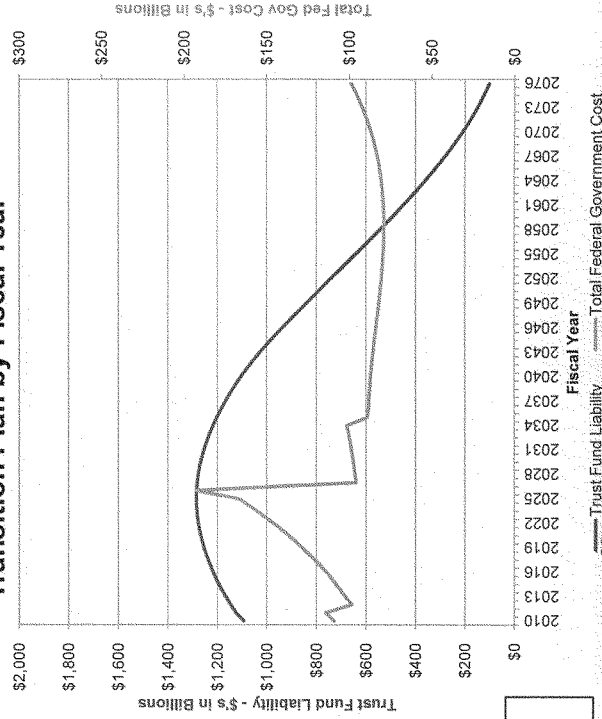
Military Retirement Trust Fund Under Transition Plan by Fiscal Year

	Today FY11*	Today's Future FY34*
DoD Service Payment	\$27.2	\$20.4
Treasury Service Payment	\$4.3	\$10.4
Treasury Interest Payment	\$21.7	\$68.5
Treasury Unfunded Liability Amortization Payment	\$61.4	\$12.5
Total Federal Government Cost	\$114.6	\$111.8
Fund Liability	\$1,125.0	\$1,217.9

*Numbers are in billions

- Assumptions:**
- Average vesting year 4
 - New recruits on new plan
 - Active duty immediately transition

Source: OSD Office of Actuary



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Written Statement of
Reserve Officers Association of the United States
and
Reserve Enlisted Association of the United States
for the
House Armed Services Committee
Subcommittee on Military Personnel
United States House of Representatives
on
The Uniformed Services Retirement System
Rayburn House Office Building
October 25, 2011



"Serving Citizen Warriors through Advocacy and Education since 1922."™



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Reserve Enlisted Association
1501 Lee Highway, Suite 200
Arlington, VA 22209
(202) 646-7715

The Reserve Officers Association of the United States (ROA) is a professional association of commissioned and warrant officers of our nation's seven uniformed services, and their spouses. ROA was founded in 1922 during the drawdown years following the end of World War I. It was formed as a permanent institution dedicated to National Defense, with a goal to teach America about the dangers of unpreparedness. When chartered by Congress in 1950, the act established the objective of ROA to: "...support and promote the development and execution of a military policy for the United States that will provide adequate National Security."

The Associations' 59,000 members include Reserve and Guard Soldiers, Sailors, Marines, Airmen, and Coast Guardsmen who frequently serve on Active Duty to meet critical needs of the uniformed services and their families. ROA's membership also includes officers from the U.S. Public Health Service and the National Oceanic and Atmospheric Administration who often are first responders during national disasters and help prepare for homeland security.

ROA is a member of The Military Coalition where it co-chairs the Tax and Social Security Committee. ROA is also a member of the National Military/Veterans Alliance and the Associations for America's Defense. Overall, ROA works with 75 military, veterans and family support organizations.

President:

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The Reserve Enlisted Association is an advocate for the enlisted men and women of the United States Military Reserve Components in support of National Security and Homeland Defense, with emphasis on the readiness, training, and quality of life issues affecting their welfare and that of their families and survivors. REA is the only Joint Reserve association representing enlisted reservists – all ranks from all five branches of the military.

Executive Director

CMSgt Lani Burnett, USAF (Ret)	202-646-7715
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DISCLOSURE OF FEDERAL GRANTS OR CONTRACTS

The Reserve Officers and Reserve Enlisted Associations are member-supported organizations. Neither ROA nor REA have received grants, subgrants, contracts, or subcontracts from the federal government in the past three years. All other activities and services of the associations are accomplished free of any direct federal funding.

The Uniformed Services Retirement System – Currently Serving

Mr Chairman and members of the committee, thank you for the opportunity to submit testimony. The manpower profile of our armed forces should be shaped by strategy rather than budget. If decisions are made in a reactive mode, more problems will be created than will be resolved. Retirement eligibility is a force shaping tool.

In 2003, the average Active Component retirement was at 21 years of service, while the Reserve Component retirement averaged 24 years. With the passage of an earlier retirement provision in 2008 providing credit for service in support of Overseas Contingency Operations, the Reserve retirement average has been reduced, more resembling that of the Active Duty.

As field experience is essential, a retirement plan should include incentives to encourage a warrior to serve longer. The current system, at least, sets the bar at 20 years.

Both enlisted and officer mid-grade shortages continue to plague the armed forces. This will be only aggravated with each service throttling back on new accessions into the services.

A proposed plan suggested by the Defense Business Board suggests that military retirement compensation be altered from a “defined benefit” to a “defined contribution” as private sector plans have done using a 401(k) style plan, allowing members of the armed forces to be vested between three to five years. This will only amplify the risk of earlier separations, as individual serving members won’t have to remain as long for retirement eligibility.

Typically, a member who stays in the armed forces beyond the initial period of active duty will be making career decisions between 8 to 12 years. A plan based on a business model could create earlier turnovers, and may actually increase federal expenses as people exit with their vestments.

With a system that encourages higher turnover, there will also be higher costs in recruiting and training, which has been estimated at over \$100,000 per recruit for primary training. Retention bonuses might have to be increased to retain certain skill sets.

To achieve savings, an immediate change would have to be made. It is inappropriate to replace the current plan for those already serving in the armed forces. The ROA and REA do not favor setting up a dual tier system where different generations of warriors involuntarily have different retirement systems. Differences between the retirement plans for the Active and Reserve Components already create enough tension as it is.

Without changing the current system, the only savings that could be accrued is by a deferment of payment. ROA and REA are not suggesting elimination of or reduction in the retirement annuity at 20 years, but suggest developing an incentive program that would be actuarially based to encourage Active Component members to delay receipt until they are older. This could be structured similar to Social Security with higher retirement annuities being paid to those who delay receipt longer. An additional incentive would be for annuity rates to annually increase at the rate of armed forces pay increases, and the High-3 formula could be calculated on the pay scale of the last three years before annuity receipt, rather than the last three years of Active Duty.

The Uniformed Services Retirement System – those already in retirement

Last September, the President announced his plan for Economic Growth and Deficit Reduction. Unfortunately, it included the recommendation to increase costs to military retirement and military families for some of their benefits. This would be a change to a compensation package that has already been earned.

Under the plan, annual fees would be instituted for TRICARE For Life health care, beginning with a \$200 annual fee in FY 2013 and would be increased annually if recommended by the Secretary of Defense. This would be above the cost of Part “B” Medicare premiums now being paid, which is means tested.

Additionally, the president suggested adjusting TRICARE pharmacy co-payments to more closely match those of Federal employee health plans by shifting retail pharmacy from dollar co-payments to a percentage co-payments, starting at 10 percent for generic drugs and increasing to 20 percent. Brand name and non-formulary drugs would start with a 15 percent copayment and would rise to 30 percent over time. Mail order generics would be free, but brand drugs would increase to a \$20 dollars co-payment and \$35 for non-formulary, with each eventually increasing to a \$40 co-payment.

Generic drugs ordered from mail order are already free as of October 1, 2011, so the president’s plan contains cost increases without offsetting incentives.

Neither ROA nor REA can support such increases. Retirees from the National Guard and Reserve would be hit the hardest because they typically retire with half of what active duty retirees receive in their pay grade.

Under a total force concept, members of the National Guard and Reserve face the same exposure to call-up, but without many of the same support programs. Many Reserve Component retirees have served in overseas contingency operations during the last ten years, or in Desert Storm. Others are veterans of World War II, Korea, Vietnam and other lesser known conflicts.

For most, retirement is tightly budgeted. Added costs are disproportionate when you are living on the margin. These retirees have earned this benefit, and should not have it altered.

Conclusion:

The serving armed forces represent less than 1 percent of the United States population with the retirees representing just another 6/10s of a percent. The sacrifices and stress faced by this group are unique, unlike anything experienced by the remaining 98.5 percent of American citizens. To target the 1.5 percent of those who have served a career in the armed forces with its included challenges to pay down the deficit is not condonable. Those who have sacrificed shouldn’t be expected to sacrifice again.

The ROA and REA are willing to work with the committee to find better ways to effectively reduce costs to not only maintain an adequate national security, but sustain the benefits of those who have served to attain it.

**WITNESS RESPONSES TO QUESTIONS ASKED DURING
THE HEARING**

OCTOBER 25, 2011

RESPONSES TO QUESTIONS SUBMITTED BY MRS. DAVIS

Dr. ROONEY and Ms. PENROD. Contracted Services are currently the largest cost element of the Total Force. The Department is committed to enhancing its understanding of what we contract for and why. For all elements of our force, we must look at whether the returns justify the investments, and if alternative Total Force mix solutions may be less costly or are more appropriate. As we have seen in the last decade, expenditures on contracted services have steadily increased, and as an element of the Total Force, must be comprehensively reviewed to ensure necessary reductions do not risk readiness and the delivery of critical capabilities. The Congressionally-mandated Inventory of Contracts for Services must continue to be improved so that it can be used by managers for these purposes.

In accordance with the FY11 authorization and appropriations acts, my office is working with all DOD organizations, to move towards collecting data from the private sector firms providing services for the Department. It is important that we have information on contracted services that can be translated to units of measure that are comparable to the other elements of our workforce (military and civilian personnel) in order to make these critical value and planning judgments.

In the past few years, we have seen the Army make judicious and highly cost-effective decisions regarding contracts governance by relying on both their inventory process and internally-developed information system. P&R has engaged to assist the Departments of the Navy and Air Force to enhance their service contracting governance ability by leveraging the Army system, as directed in the FY11 appropriations act. Additionally, we are also assisting the Defense Agencies, Field Activities, and Combatant Commands as they report their plans to collect this information. This year, the Components will prepare an improved FY2011 Inventory of Contracts for Services by relying on the best information they have available in their internal systems as opposed to the Federal level aggregated reporting system, while leveraging the Army's proven processes and data.

Finally, my office has drafted guidance that will be soon released Department-wide. This guidance will require, in addition to an improved inventory, that each DOD Component complete a thorough review and analysis of the contracted services for which they are the requiring activity, and will require the Component Head to submit a letter to my office certifying completion of such review, delineating the results in accordance with all applicable Title 10 provisions. This additional accountability will ensure each DOD Component can report workforce mix decisions and that contracted services are validated against mission requirements that justify current and proposed expenditures during annual program and budget reviews, and that corrective action is taken when functions at risk of inherently governmental performance or involving unauthorized personal services are identified. [See page 22.]

RESPONSE TO QUESTION SUBMITTED BY MR. COFFMAN

Dr. ROONEY. The Defense Department annually contributes into the Military Retirement Fund a portion of the actuarially determined amount required to pay retired pay to future military retirees; the Treasury Department pays the remainder of the actuarially determined amount.

For the 2012 fiscal year, the Defense Department contributed an amount equal to 34.3 percent of active component military basic pay to fund retired pay for future active duty retirees and 24.3 percent of reserve component military basic pay to fund retired pay for future reserve component retirees. It is projected that these contributions, as a percentage of military basic pay, will remain relatively constant well into the future.

In FY 2012, the Treasury Department contributed to the Military Retirement Fund 8.8 percent of active component military basic pay and 3.6 percent of reserve component military basic pay. The Treasury Department's portion represents the cost of "concurrent receipt" benefits first enacted in 2004. [See page 12.]

QUESTIONS SUBMITTED BY MEMBERS POST HEARING

OCTOBER 25, 2011

QUESTIONS SUBMITTED BY MS. BORDALLO

Ms. BORDALLO. How can the Department consider “breaking faith” with the troops and propose drastic reforms to retirement and benefits to the military’s all-volunteer force to meet declining budgets, while at the same time failing to achieve a realistic accounting of expenditures on contracted services, which have increased drastically in the past decade? In fact, for nearly half of that decade, the Department has failed to implement a required inventory of contracts for services, directed by Congress in FY08 NDAA. P&R was directed, twice in fact, in the most recent legislative cycle to take specific and deliberate actions to move the Department forward in that area. Without this critical tool, how can the Department control costs in a time of fiscal austerity, reducing military and civilian end-strength, but ignore the work performed by contractors? Wouldn’t this be a more natural first choice for identifying budgetary savings than at the expense of “breaking faith” with our dedicated men and women in uniform?

Dr. ROONEY. While it is accurate that possible retirement and compensation reforms are being considered, the Department is still in the very early stages of developing any potential options for such reform and no decisions have been made. The Secretary and I, along with many other senior leaders, take very seriously the commitments we’ve made to our men and women in uniform and we will not break faith with those service members. Any proposed reforms and changes to retirement will contain a requirement for grandfathering.

I agree that work performed by contractors comprises a significant portion of the Department’s budget that must be reviewed in order to achieve balanced, meaningful and lasting savings and cost reductions. To that end, we are committed to enhancing our understanding of the services we contract for and why, and how much we spend on those services. The Inventory of Contracts for Services must continue to be improved so that it can be used as a tool by managers for these purposes. In accordance with the FY11 NDAA and the recent appropriations bill, my office is working with all DOD organizations to move towards collecting data related to level of effort and costs from all private sector firms providing services for the Department. On November 22, the Department delivered to the Congressional defense committees a plan that delineates both short and long term actions to be taken by the Department to begin collecting data from private sector firms and fully comply with requirements of sections 235 and 2330a of title 10, United States Code. It is important that we have information on contracted services that can be translated to units of measure that are comparable to the other elements of our workforce (military and civilian) in order to make critical value and planning judgments. With the right data, opportunities for savings can be identified, thus ensuring that returns justify investments. The data will also assist in promoting alternative workforce solutions that may be less costly and more appropriate, or eliminating or reducing in scope those services determined to be no longer required or of low priority.

Ms. BORDALLO. In this hearing there was a lot of discussion about comparison between the military and private sector employment, specifically the specialized training, physical attributes, and sacrifices made by uniformed men and women that ensure a constant state of readiness. As we reduce our operational tempos overseas, and drawdown those force levels, what is the Department doing to ensure that military men and women are not being placed into jobs that do not contribute promote unit readiness or further their careers, and consequently generate a hollow force? This is of particular concern as the Department operates under a civilian personnel constraint and there are thousands of control grade officers in headquarters or administrative type functions that may be better suited for civilian performance?

Dr. ROONEY. The Department’s “sourcing” of necessary functions and work between military, civilian, and contracted services must be consistent with workload requirements, funding availability, readiness and management needs, as well as applicable laws. As operational tempos in Iraq and Afghanistan decrease and the Department makes force structure adjustments, military personnel availability will certainly be a consideration in workforce structure decisions to most effectively and efficiently perform the missions, including those at headquarter staffs and of an administrative nature. In making such staffing decisions, the Department must be

mindful of using military personnel to perform tasks that could limit their availability to perform the operational missions or maintain a required state of readiness.

Consistent with DOD policies, tasks that are not inherently governmental or military essential in nature must be designated for Government civilian personnel or contract performance unless military-unique knowledge and skills are required for performance of the duties; military incumbency is required by law, executive order, treaty, or international agreements; military performance is required for command and control, risk mitigation, or esprit de corps; and/or military manpower is needed to provide for overseas and sea-to-shore rotation, career development, contingencies or wartime assignments.

My staff has currently begun a study to review the grade/billet appropriateness and allocation of control grade officers. This study may result in more in depth reviews of military billets at headquarters and administrative functions and activities across all organizations of the Department. Among other things, consideration for military to civilian conversions or organizational efficiencies that will reduce military personnel performing overhead activities will reduce the likelihood of hollowing the force.

Ms. BORDALLO. Much attention has been paid to the role of contractors in theater—as well as the sustainment, infrastructure, and maintenance support provided to the Department by the private sector. However, as we shape the force of the future and discuss the likely impact the possibility of retirement and compensation reforms will have on the Department's ability to recruit and retain a ready and capable force, what steps are being taken to ensure that the future mix of the Department's workforce is appropriately balanced? Declining end-strengths and civilian personnel limitations would seem to lead to a “default” of contracted support to meet future operational needs (similar to the post 1990s drawdown). What controls are being implemented, related to contracted service levels, to preclude favoring one element of the Total Force over another?

Dr. ROONEY. As a result of fiscal constraints and declining budgets, the Department is assessing all aspects of its Total Force, including contracted support. These assessments may result in force structure changes, organizational realignments and restructuring, workload prioritization, and the identification of lower priority mission/functions for elimination. As part of these assessments, workforce structure decisions must be consistent with workload requirements, funding availability, readiness and management needs, and applicable laws. Decisions regarding the use of military personnel, Government civilians, or contract support must follow workforce mix and risk guidance in DOD Instruction 1100.22, “Policy and Procedures for Determining Workforce Mix”, and, when appropriate, cost considerations in accordance with Directive Type Memorandum 09-007, “Estimating and Comparing the Full Costs of Civilian and Military Manpower and Contract Support.”

In addition, the Department has prepared policy reiterating and reinforcing statutory prohibitions against converting work currently performed (or designated for performance) by military and civilian personnel to contracted services. This policy highlights the importance of preventing the inappropriate conversion of work, or “default” to contract performance.

Lastly, the Department is committed to enhancing its understanding of current and planned services contracts. On November 22, the Department delivered a plan to the Congressional defense committees that delineates both short and long term actions for the collection of data from private sector firms. These actions will improve the Department's ability to assess contracted services in a manner comparable to the other elements of our workforce in order to make critical value and planning judgments, as well as precluding unjustified or unintended growth in this sector of the Total Force.